UNITED STATES BANKRUPTCY COURT

SOUTHERN DISTRICT OF NEW YORK

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In the Matter of:

LEHMAN BROTHERS HOLDINGS INC., Case No. 08-13555-scc

Debtor.

- x

United States Bankruptcy Court

One Bowling Green

New York, New York 10004-1408

November 20, 2017

10:00 AM

B E F O R E:

HON. SHELLEY C. CHAPMAN

U.S. BANKRUPTCY JUDGE

IN RE: RMBS Claims Estimation Trial

Transcribed by: Dawn South, Sheila Orms, Lisa Beck

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P R O C E E D I N G S

THE COURT: Good morning.

(A chorus of good morning)

THE COURT: Please have a seat. Well here we are at last. How's everybody?

MR. COSENZA: Good.

THE COURT: Good.

Okay. So just to confirm how today is going to proceed. You had allotted two hours each for openings, yes?

MR. COSENZA: Roughly, Your Honor, and you know, plus or minus, but that's -- yes.

THE COURT: Plus or minus, depending upon how much I talk.

MR. COSENZA: Yes.

THE COURT: Okay. And the trustees go first?

MR. COSENZA: No, we go first.

THE COURT: You go first.

MR. COSENZA: We go first, Your Honor.

THE COURT: That was by agreement?

MR. COSENZA: Yes.

THE COURT: That was by agreement.

Okay. So the idea is going to be, Mr. Cosenza, that you will argue before lunch and then we'll take a break.

MR. COSENZA: Correct. Sounds good, yes.

THE COURT: Good. So that we don't have Mr. Shuster feeling lightheaded while he's making his argument.

So there are a whole host of other issues that we need to discuss. My preference would be to put those to the side and we have our arguments, and then after Mr. Shuster concludes this afternoon we can take up all outstanding issues and talk about other issues that we've accumulated along the way.

MR. SHUSTER: And I do not intend in my opening to refer to any of the material that's in dispute.

THE COURT: That's in dispute.

MR. COSENZA: Okay.

THE COURT: All right, Mr. Cosenza?

MR. COSENZA: That's fine, Your Honor.

THE COURT: I'd much preferred to that and get us off to a good start.

MR. COSENZA: May I approach, Your Honor?

THE COURT: Please.

(Pause)

MR. COSENZA: Your Honor, I'm just handing up a slide deck.

THE COURT: Okay.

MR. COSENZA: It's part of the opening.

THE COURT: Thank you. Ready when you are.

MR. COSENZA: Okay. Great.

May it please the Court, Todd Cosenza on behalf of the plan administrator.

Your Honor, the plan administrator is responsible for, among other things, resolving disputed claims so that those claims are allowed at the appropriate level and creditors may receive distributions under the Chapter 11 plan.

As the Court knows the plan administrator has been working hard to resolve disputed claims at fair levels and in an expeditious manner.

Consistent with that mandate we are here on the plan administrator's motion under Section 502(c) of the Bankruptcy Code to estimate the amount of the RNBS trustees remaining claims had the claims protocol been completed.

THE COURT: Can you say that again, Mr. Cosenza?

MR. COSENZA: Sure. Sure. So we are here to estimate the amount of the RNBS trustees remaining claims had the claims protocol been completed.

THE COURT: Do the trustees agree with that formulation of the issue?

MR. COSENZA: Yes.

THE COURT: Okay.

MR. COSENZA: Thank you.

In a Section 502 estimation proceeding the Court's

principle consideration in estimating a claim should be to promote a fair distribution to creditors to a realistic assessment of uncertain claims.

There's no dispute that estimation under 502 is appropriate here. In fact both sides have agreed to ask the Court to estimate the claim to further insure an expeditious final resolution.

As both sides agree, estimation is appropriate because it would be virtually impossible, Your Honor, for the Court to hear and determine all the remaining 107,000 underlying disputed claims on 70,973 loans still in dispute.

It will be clear that the trustees' evidence will not be sufficient to carry their burden to prove claims in excess of the $300 million of claims the plan administrator has passed to date as a result of the protocol. Nevertheless, the plan administrator stands behind the terms of our settlement agreement with the trustees and institutional investors. We are just asking the Court to estimate the claims at $2.38 billion.

As Your Honor knows both sides have agreed not to pursue a sampling methodology to establish the quantum of the trustees' claims, thus in the absence of a trial on all the claims by sampling or otherwise the plan administrator believes the Court will need to assess a number of guideposts to determine the appropriate level for these

claims.

As the evidence will show there are many guideposts that all lead to a claim of $2.38 billion or less. The RNBS trustees maintain that their protocol process has resulted in a claim of $11.4 billion. Not one guidepost would direct the Court towards a conclusion that the RNBS trustees' claims could ever be anywhere near the $11.4 billion that they are seeking here. In fact it would generate an enormous windfall at the expense of all other creditors. The plan administrator believes that fuller guideposts lead to a claim amount of $2.38 billion or less.

Your Honor, I will come back to all of this at the end of my presentation, but let me give you a brief overview now.

The first guidepost is that the $2.3 billion that the plan administrator is asking Your Honor to estimate the claim at is equivalent to a settlement negotiated in October 2015 with the institutional investors. The settlement was reached with the largest and most sophisticated of Lehman investors of Lehman RNBS.

The institutional investors moved the plan administrator to the very top end of our range for these claims, $2.44 billion, and that is where the plan administrator elected to resolve these claims at after our negotiations with the institutional investors.

The second guidepost is that the 2.3 billion is at the high end of various comparable global RNBS settlements.

In support of this guidepost Your Honor would hear testimony from Professor Daniel Fischel. By the way, Professor Fischel has acted as an expert for the trustees in connection with RNBS settlements they have sponsored.

Here he will testify that the recovery of $2.38 billion here as a percentage of expected lifetime losses for the trust at issue, which he will refer to as the recovery ratio, is 11.2 percent. Again, the plan administrator will show that the recovery ratio is at the high end of the range of recoveries as compared to these global RNBS settlements as reflected in this chart.

The evidence will show that what the trustees are seeking, $11.4 billion, is far outside the range of all other big bank global RNBS settlements and would result in a recovery ratio more than four times the highest recovery rate set forth on this chart.

The third guidepost is a pricing or value that the trustees have themselves ascribed to their claims in connection with six terminated trusts.

As the Court is aware, and as we described in our brief, since the RNBS settlement was reached between the trustees, institutional investors, and the plan administrator a number of trusts that were subject to these

proceedings have been cleaned up by the master servicer and those trusts have been terminated. These are the six trusts. And the RNBS trustees are no longer prosecuting these claims because the trustees of the claims that have been asserted in this proceeding -- sold -- sorry -- sold these claims that have been asserted in the proceeding to the master servicer and the clean up process.

Now, did the trustees sell the claims to these six trusts based on the claim amount the trustees have proposed to be allocated for each trust based on the trustees' protocol output, the $11.4 billion that the trustees are seeking here? The answer is no. The trustees sold these claims at a value equivalent to each trusts allocable share of the amount that the plan administrator is seeking estimation here, $2.38 billion.

If the trustees thought that 11.4 billion was a fair proxy of value, how could they allow the claims to be sold at $2.38 billion level for these 6 terminated trusts? As fiduciaries the trustees could not.

The fourth guidepost is Dr. Cornell's (ph) analysis. Dr. Cornell, who Your Honor will hear from in our rebuttal case, is a leading expert in the fields of structured finance and valuation of RNBS.

The plan administrator provided generous assumptions to Dr. Cornell on the trustees' likelihood of

success on their claims here. Dr. Cornell assumed the inflated purchase price calculations and assumed the generous excess assumptions provided by the plan administrator. Using that information Dr. Cornell will opine that the trustees' recovery on a loan by loan basis would result in a claim within the range of $1.6 billion to $2.5 billion. In contrast we are confident that the evidence will uncover that the trustees cannot support their $11.4 billion claim.

In addition to the guideposts I've outlined the evidence will show in particular first that the trustees had a fundamentally flawed approach to the protocol.

Second, the trustees failure to carry their burden of establishing proof. As the trustees have conceded they must prove that the loans at issue contain actual breaches that have an adverse and material effect on the value of the loan now when they brought their claims.

And third, the trustees grossly -- sure.

THE COURT: Before you go to the third bullet point. So the plan administrator is not conceding any deemed AMAs for any type of breach?

MR. COSENZA: There are some deemed AMAs, Your Honor, that we did approval during the protocol, but there are some deemed AMAs that are still I believe at issue.

THE COURT: Thank you.

MR. COSENZA: Next the trustees grossly overstate their damages. Again, Your Honor, this includes among other things, their use of the full purchase price, which I will explain in more detail later.

Second, the trustees' unreliable methodology to calculate losses on active loans. These are loans, Your Honor, that are still performing to this day, although they may have been modified or changed in some sense.

And the trustees' wrongful inclusion of both prepetition and post-petition unmatured interest.

I would now like to frame these issues before the Court with just a little bit of history.

As Your Honor is aware the plan administrator has been trying to resolve these claims in different ways for years, both through settlement discussions and mediation. The efforts began after the Lehman's bankruptcy filing on September 15, 2008, and the trustees filing of over 300 proof of claims in 2009 through which the trustees sought to recover billions of dollars across approximately 405 trusts.

The proofs of claims suffered from fundamental defects. The proof of claims did not provide notice of any individualized loans nor evidence of any damages allegedly caused.

From 2010 to 2014 the plan administrator made it crystal clear that we required proof on a loan by loan basis

to consider these claims for allowance. Having not received this proof the plan administrator moved in June 2011 to disallow and expunge the claims brought by the RNBS trustees. Although at the time Judge Peck reserved decision on most of the claims, he recognized that the governing agreements required the trustees to put forth individualized proof for each claim put forward.

As Judge Peck stated:

"If there are claims the trustees would be put to their proof and whether they can actually succeed in carrying a burden of proof establishing residential and mortgage loan breaches would be extraordinarily difficult."

The plan for Lehman was confirmed in December 2011.

And from 2012 to 2014 the plan administrator negotiated directly with the RNBS trustees and engaged in mediation in an attempt to resolve these claims. Again, the mediation process failed.

Then in August 2014 the trustee sought to increase the reserve for these claims and estimated and allowed the claims in an amount to be determined after an estimation hearing. The trustees argued that their claims were worth no less than $12.143 billion based on a flawed sampling methodology. The trustees however had not actually

identified the specific loans at issue or submitted proof of the loans alleged breaches.

In response the plan administrator requested in October 2014 the implementation of a protocol intended to provide a process giving the trustees first, time to gather and identify valid claims and submit sufficient detailed proof for these claims.

Second, a process for resolution of each claim at a fair level in non-legal business person to business person meetings.

Third, a mediation forum for compromise or resolution of each claim.

Fourth and finally, and only if necessary, a resolution by the Court at trial on each remaining loan.

After a hearing on December 10th, 2014 the Court indicated and wanted the protocol process to move forward.

The parties then negotiated the terms of the protocol and the Court entered the protocol order on December 29, 2014. And Your Honor told the trustees that the Court was available to assist in any way with the trustees' collection of the documents required under the protocol.

From March 2015 through March 2017 the parties then engaged in the protocol process. The parties also provided status updates to the Court during that time

period. Again, as Your Honor is aware, the trustees flooded the protocol with over 193,000 claims relating to 94,566 loans. Again, many of the claims submitted by the trustees were unfounded and were unsubstantiated.

This overwhelming submission of so many unfounded claims also undermined the purpose behind the claims resolution process in the protocol order. The protocol was intended to fairly and efficiently resolve most of the claims without the need for a trial. The trustees' submissions also contravene the express words of the protocol order which required the trustees to have a "good faith basis" for every claim the trustees put forward. However, despite these challenges the plan administrator remained committed to resolving the claims fairly and efficiently.

In 2015 the plan administrator reached out to the trustees largest beneficiaries through their counsel. This was a group of 14 institutional investors, including among them Goldman Sachs Asset Management, Black Rock, AGON, PIMCO, MetLife, and LAMCO. This group represents some of the largest and most sophisticated investors in structured finance and products.

These institutional investors are the parties with a real financial interest in the claims, unlike the trustees. The institutional investors also have

significance experience resolving RNBS claims of similar scope and magnitude involving the trustees here, and I will detail that later.

After engaging in negotiations for several months the plan administrator and the institutional investors struck a deal in October 2015. As part of the deal the institutional investors agreed to accept 2.44 billion for their covered RNBS claims, subject to this proceeding, as well as a transfer of loan RNBS claims. As Your Honor is aware the transfer of loan RNBS claims have been dealt with in a separate proceeding.

The agreement was presented to the trustees for consideration and approval; however, the trustees' unwillingness to exercise discretion again frustrated the deal. The trustees would not accept a deal for a sufficient number of trusts based on a purported expert report. As the Court is well aware the trustees to this day steadfastly refuse to fully disclose that report.

Undeterred the plan administrator continued its efforts to try to resolve these claims as efficiently and fairly as possible.

As the protocol continued and the trustees continued to make an overwhelming number of claims and take aggressive and unsubstantiated positions, the plan administrator renewed discussions with the institutional

investors in the summer of 2016. This resulted in a settlement with the institutional investors in November of 2016 to establish a process to estimate the trustees' covered loan claims.

After much negotiation with the trustees and revisions to the agreement the trustees finally accepted the revised settlement agreement on June 1, 2017, which established the procedures for this estimation hearing.

After a 9019 hearing on July 6th, as the Court is aware, the Court approved the revised settlement agreement over a handful of objections that were subsequently resolved or withdrawn.

Again, as the Court is aware, the settlement establishes a streamline process to resolve the trustees' covered loan claims submitted through the protocol.

It is not in dispute that the settlement provides "numerous benefits to creditors, including providing a framework for a prompt determination of the covered loan claims in a fair and reasonable manner before this Court."

From the plan administrator's perspective it is critical because it satisfies our objective of a timely and fair resolution of the claims and attempts to insure that this matter will be resolved before the next plan distribution in March 2018.

Under the terms of the agreement the plan

administrator agreed to seek estimation at $2.416 billion, which is now adjusted to $2.38 billion based on various subsequent events to the entering of the settlement agreement.

It is important to note that while the plan administrator is seeking to estimate the claims at 2.38 billion Your Honor is free to determine the correct amount based again on the evidence presented.

The plan administrator believes and will present evidence that the $2.38 billion amount represents a fair estimation of the trustees' claims had the trustees properly complied with the protocol order.

Based upon what the plan administrator has learned of the trustees' claims and their process during our preparation for this estimation hearing the plan administrator believes the trustees' claims and process was so riddled with flaws that the trustees may only be able to prove or meet their burden to prove claims at a value of $300 million.

However, pursuant to the plan administrator's obligations under the settlement agreement with the institutional investors and the trustees we ask the Court to estimate the trustees' claims at $2.38 billion.

The plan administrator acknowledges that this places it in an odd position. We are seeking a claim value

substantially higher than what we believe the trustees' evidence will support based on their flawed process during the protocol. On the other hand we also believe the 2.38 billion represents a fair estimation and resolution of these claims in an expeditious manner for both the plan administrator and the institutional investors.

Your Honor, some of the unique features -- again, you're aware of much of this -- of the RNBS settlement agreement and process are first, each side has 49 hours to present their case. Other settlement agreements and disputes involving RNBS are allowed into evidence. The October 2015 settlement for $2.44 billion between the plan administrators and institutional investors is also allowed into evidence. And there are limited appeal rights. The plan administrator has waived its right to appeal to insure the results from this proceeding can be reflected in the March 2018 plan distribution. And the trustees may appeal only if the Court determines the trustees' proven claims are valued at less than $2 billion.

Your Honor, the plan administrator is sympathetic to the challenge facing the RNBS trustees and has always tried to be reasonable. The number and complexity of the transactions underlying these claims are significant.

As the Court is aware we started with 405 different trusts populated with hundreds of thousands of

mortgage loan files, each having unique and diverse characteristics. Again, this estimation proceeding is intended to establish the value of the claims that would have been resolved in steps three through five of the protocol if the parties hadn't entered into this settlement agreement.

The plan administrator is trying to be fair by seeking estimation at the $2.38 billion level. We were trying to resolve the trustees' claims, which is one of the largest outstanding claims against the estate expeditiously. Again, this is why the plan administrator entered into this streamline process so the results could be reflected in the March 2018 distribution. Yet the trustees have taken the opposite approach, they seek a windfall by requesting a claim of $11.4 billion.

To be clear, to get to the $11.4 billion that would mean that the trustees had met their burden in the protocol for every element of their claim for all 70,973 loans remaining at issue, and according to the trustees they have no obligation for any of these claims to show any an nexus between the breaches they allege and the damages they seek.

The trustees have the burden of proving entitlement to more than 2.38 billion that the plan administrator seeks to estimate the claims at. The evidence

will show the trustees cannot do that. And the evidence will show that they cannot show entitlement to the $11.4 billion they are seeking here.

THE COURT: So the $11 billion figure, that ties out to a 100 percent success rate with respect to the remaining loans in the pools?

MR. COSENZA: Correct, Your Honor.

THE COURT: And in order to get to that -- so there are multiple breach -- for example, let's take a loan.

MR. COSENZA: Yeah.

THE COURT: There might be multiple breaches asserted with respect to a loan, right?

MR. COSENZA: Correct.

THE COURT: So hypothetically that would mean that the trustees would need to prevail -- would only need to prevail -- well this is a question I guess.

MR. COSENZA: Yes.

THE COURT: They would only need to prevail on one breach in order to prevail on that loan or alternatively in order to demonstrate an AMA they might need to prevail on more than one breach. I'm asking.

MR. COSENZA: That's correct, Your Honor. I mean just as a --

THE COURT: In broad outline.

MR. COSENZA: Yes, in broad terms you're correct.

For example, and I'll just throw out a hypothetical here. If there's a missing document claim --

THE COURT: Yes.

MR. COSENZA: -- that may have been there at origination that went missing and they're pursuing that claim in this proceeding and they're able to sustain their burden on that file and there's a breach in theory they have proven that that document should have been there and it's a missing document claim. Whether or not they have proven AMA and whether or not they have proved that they're entitled to the full damages based on the purchase price that's --

THE COURT: But the --

MR. COSENZA: Yeah.

THE COURT: -- but the $11 billion number assumes a win --

MR. COSENZA: Yes.

THE COURT: -- on every loan --

MR. COSENZA: Correct.

THE COURT: -- remaining.

MR. COSENZA: Correct.

THE COURT: Okay. Thank you.

MR. COSENZA: Your Honor, it is our understanding that the trustees -- and this is based on their pretrial brief -- will try to meet their burden by presenting certain loans supported with general categories of proof. Based on

these protocol exemplar loans the trustees will ask the Court to extrapolate to the entire pool of loans and claims based on the trustees' loan review process. The evidence will show however that the trustees will not be able to do that because the trustees' process was fundamentally flawed and unreliable.

Without having a sound and reliable process the plan administrator believes that the trustees will attempt to put forward an exemplar loan and then use certain types of evidence to support a certain type of breach on that loan.

Whatever the evidence will show for that particular loan and whether the trustees have sustained their burden on their breach claim for that loan will be up to the Court.

What does not work here in the context of these unique files with different factual circumstances and evidence is to take whatever conclusion is reached on that one loan file and extrapolate it out through thousands of loan files containing the same alleged breach that relies on similar evidence.

THE COURT: Okay. So this is an extremely important point. So exemplar sounds a lot like sample. Same Latin root or whatever it is, right?

MR. COSENZA: Yes.

THE COURT: But we're not doing sampling, right?

MR. COSENZA: That's correct, Your Honor.

THE COURT: And we're also not -- this a question -- we're also not over the next couple of months seeking to create a record with respect to loan by loan proof, right?

MR. COSENZA: That's correct, Your Honor.

THE COURT: So we're estimating, but we're not sampling, but we're using exemplars.

MR. COSENZA: That's correct. And -- well our argument will be on that point, Your Honor, is the exemplar approach could be successful if there's --

THE COURT: If the -- if it could be proven --

MR. COSENZA: Yes.

THE COURT: -- that the process was close to impeccable.

MR. COSENZA: Yes, that's correct, Your Honor.

Indeed, Your Honor, we're going to present evidence and loan files that show that the facts and circumstances underlying each loan file is unique. So the evidence will show the trustees have a good process, which they did not, the type of generalized proof they are using to support a certain breach type will not be sufficient to carry the trustees' burden of proof on each of the 70,973 loans at issue.

Furthermore, under the trustees' theory of the

case a breach automatically entitles them to compensation at the full purchase price under developing governing agreements. But, Your Honor, this is not a repurchase case. As the trustees pointed out in the very first sentence of their pretrial brief, "Each claim brought here, 107,000 claims on the 70,973 loans, is a 'straightforward breach of contract claim'" And that's from the trustees' brief.

The trustees are seeking breach of contract damages, not the repurchase of the loan.

I will address this in more detail later, but the highest level here are the contractual elements the trustees must prove for a valid claim under the governing agreements.

One, that there was a material breach of a representation and warranty.

Two, that the breach adversely and materially affects the value of the loan at the time notice is given. And as the plan administrator noted in its pretrial brief, affects is used in the present tense, in other words affect at the time a claim is made by the trustees, and that will be important for reasons I will explain later, Your Honor.

And three, that the entirety of the amount of damages claimed is compensable under applicable law.

The evidence will show that the trustees failed to meet their burden during the protocol and that the $11.4 billion they are seeking is baseless.

Moreover, the $11.4 billion figure ignores the billions and billions of dollars in interest that the certificate holders have received on these loans since the trust's inception and since Lehman's bankruptcy. This is especially unfair when one considers that the trustees have nowhere acknowledged that they have been collecting interest payments on all of these loans since the trust's inception in the magnitude of billions of dollars. Most of this again since Lehman's bankruptcy.

Your Honor will hear testimony that the plan administrator implemented a sound process to assess each loan file and claim submitted during the protocol and attempted to treat these claims fairly.

We would note, Your Honor, that the plan administrator -- and I've said this throughout my numerous status conferences before the Court -- that we had an extremely difficult and demanding task given the extraordinarily large number of claims the trustees put forward in the protocol.

I'd now like to describe for the Court how the parties got to the number of loans that are in dispute here today, because these numbers seem to be jumping around in terms of loans that went through the protocol or not so I'll just provide you with a little bit of background.

Since the settlement was entered in March 2017, as

we'll discuss later, the trustees have abandoned approximately 15,570 loans and 73,245 claims. The pool of loans and claims at issue has also been diminished due to the collapse of several trusts and opt out and loans that have paid out in full.

So as I mentioned earlier, Your Honor, you will hear that despite the protocol requiring the trustees to submit their claims based on a good faith determination that the relevant claim files contained material breaches, the evidence will show that the trustees did not do that.

Indeed as we noted during our various status conferences the plan administrator was concerned about the volume and quality of the loans and claims that the trustees were putting through the protocol; however, the trustees made various representations to the Court about the high quality of their process and the validity of every claim submitted during the protocol process.

For example, and there are numerous examples of this, in a September 2015 conference before Your Honor when the plan administrator challenged the volume and types of claims the trustees were putting forward that were bogging down the protocol process the trustees' counsel repeatedly defended the quality of the claims the trustees were putting through the protocol. In fact the trustees claim they were "very measured in coming up material breaches," they also

told the Court that their process included a "quality control program, and that all the claims asserted in the process -- protocol process were strong."

The evidence will show that the plan administrator was correct about the poor quality of the trustees' claims. As we now understand the trustees have abandoned over 73,000 claims that were put through the protocol. We believe this demonstrates that the trustees' process was fundamentally flawed.

As the Court is aware when we asked for an explanation for the dropped claims back in July of this year the trustees maintained the decision to drop the claims for "by attorney/client privilege." This is evidenced, Your Honor, by a July 24, 2017 letter that is up here.

In that letter the trustees informed the plan administrator that they would not provide any information concerning the timing and rationale of the trustees' decision to drop these claims and loans.

The trustees asserted, and you can see from this letter, that they were under no obligation whether pursuant to Exhibit G, the protocol, or other authority to provide information concerning confidential and privileged discussions, they will not do so. And the trustees also told the plan administrator in that letter that they would not produce any witnesses to testify about this issue.

The trustees followed through with this at all the depositions. Whenever the plan administrator asked the trustees' witnesses about withdrawing loans and claims the trustees steadfastly blocked discovery on the timing and rationale to drop these claims and always invoked attorney/client privilege. This is remarkable.

Your Honor, both parties will present evidence to support that their approach to the protocol process was more likely to yield the appropriate number of compensable claims under the governing agreements. Hereto the parties have taken two different approaches to how they will present the evidence.

First, the plan administrator will present testimony from Mr. Zachary Trumpp, who supervised the plan administrator's review of the trustees' claims submissions during the protocol. Mr. Trumpp was involved in this matter from the beginning, Your Honor.

You will hear him testimony that the plan administrator repeatedly requested loan level evidence sufficient to support each of the proofs of claim but the trustees never provided it.

Determined to help bring these claims to resolution Mr. Trumpp helped develop the protocol. He was also responsible for assembling the teams used by the plan administrator that performed the loan review during the

protocol.

In assembling, implementing, and overseeing the protocol for the plan administrator Mr. Trumpp brought significant experience in the mortgage loan industry.

Prior to the protocol Mr. Trumpp created and managed the lost management department at Aurora Loan Services, which identified and pursued claims against loan originators.

Post bankruptcy Mr. Trumpp has overseen the plan administrator's pursuit of recoveries on behalf of creditors for mortgage loans on which LBHI suffered losses.

Therefore, long before the protocol Mr. Trumpp was well versed in all aspects of identifying, evaluating, and pursuing claims associated with breaches of representations and warranties.

Importantly, Mr. Trumpp also knows from his experience what type of claims for breaches of representations and warranties typically are not pursued in the mortgage industry.

Mr. Trumpp's years of experience taught him that the outcome on a particular claim always depends on the facts and circumstances of a particular loan and the language of the governing agreements, which typically vary from case to case.

Mr. Trumpp will testify that during the protocol

process the plan administrator's teams reviewed each loan file individually and undertook an analysis of all of the relevant information in that loan file to determine whether the information the trustees submitted supported the elements of a breach. This effort was extraordinarily challenging because of the number and types of claims the trustees put forward in step one of the protocol, over 193,000 claims and the lack of evidence the trustees provided.

In an attempt to spin this the trustees make a rather strange assertion in their pretrial brief that the plan administrator did not refute the trustees' proof on each loan during the protocol process. This spins the protocol on its head by attempting to invert the burden of proof.

The trustees as an initial matter and as I described earlier, did not make a "good faith determination" on what types of claims they submitted and the types of evidence they put forward. Instead they flooded the protocol in step one with an overwhelming number of claims. That put, as I mentioned earlier, the plan administrator in a bind, and the trustees' assertion that the plan administrator did not provide sufficient responses is also inaccurate.

Your Honor, you will hear from Mr. Trumpp next

week. He will testify about the totality of the communications between the plan administrator and the trustees during step two and three of the protocol, which belie the allegations made by the trustees their brief.

Your Honor will also hear testimony from an independent expert the plan administrator retained, Mr. Charles Grice.

Mr. Grice audited a broad subset of the trustees' breach claims and the plan administrator's responses.

Mr. Grice will testify that based on his extensive experience in the residential lending industry reviewing mortgage loan files, analyzing claims of breaches of representations and warranties, and conducting quality control audits of loan reviews processes, that he believes the plan administrator's process was sound and constructed to maximize the likelihood that the plan administrator would reach the appropriate result on each claim and loan.

He will also testify based on his audit of a broad subset of the trustees' breach claims and the plan administrator's responses that there were fundamental and significant deficiencies in the trustees' breach analysis.

Mr. Grice will testify that this shows that the trustees' process and procedures would tend to produce unreliable results.

Mr. Grice will explain that the trustees'

conflated relevance will sufficiency. This false equivalency largely defines a difference between the trustees' position and the plan administrator's position on the burden of proof just on the breach of claims issue, Your Honor.

After hearing about the plan administrator's process Your Honor will hear next what the trustees did during their loan review process.

THE COURT: Is Mr. Grice, does his testimony cover both the issue of material breaches and adverse material effect or only the materiality of breaches?

MR. COSENZA: Only the material breaches, Your Honor. Mr. Castro, who I'll describe later, is covering the AMA issues.

After hearing about the plan administrator's process Your Honor will hear what the trustees did during their loan review process.

Your Honor is aware the trustees hired Duff & Phelps to manage their loan review process under the protocol. Mr. James Aronoff, who was at Duff & Phelps, testified regarding his extensive role in the trustees' protocol process. Here are Mr. Aronoff's own words as he describes his role in the protocol.

(Video deposition played)

MR. COSENZA: So Mr. Aronoff testified he was

quote/unquote, the boss of the team responsible for managing the trustees' loan review. Not only was Mr. Aronoff the boss of the trustees' process, he was also responsible -- and this is from his own testimony -- for the "substantive aspects of the forensic loan reviews," which included -- according to Mr. Aronoff -- "both the breach findings and the determinations whether those breach findings adversely and materially effected the value of the loan, among other things."

Mr. Aronoff was also responsible -- again, this is according to his own testimony -- for "the sufficiency or the use -- the appropriate use of any particular form of supporting information or documentation as a basis for the identification of a breach finding." And in his words, "as well as getting involved in the interpretation of various informational sources, breach findings, scope of the reps and warranties that amount to those breach findings, and the like." So that's at a mouthful, but I'm trying to get through it quickly.

As Your Honor will hear Mr. Aronoff also was the final decision maker on whether breaches satisfies the adverse material effect or AMA element for the majority of the loans submitted in the protocol.

Let's hear from Mr. Aronoff on this.

(Video deposition played)

MR. COSENZA: So Mr. Aronoff was intimately involved in the trustees' process to review the loan files. That is not disputed, Your Honor.

Despite his integral involvement in the process Mr. Aronoff will be testifying as an expert as to the validity of the trustees' representation of warranty breach findings.

Mr. Aronoff has been put in an incredibly awkward position of now being retained to opine on the process he designed and oversaw. Indeed he's playing a very odd hybrid role here, which by definition lacks objectivity. Not only is Mr. Aronoff a critical fact witness, but the trustees have retained him as their expert.

Your Honor, I have never encountered this in my many years of practice, and it's quite odd that he'd be serving as an expert on this. Frankly this is no different than an attorney accused of malpractice testifying as an independent legal expert at his own malpractice trial. But Mr. Aronoff is not independent and cannot be an objective witness about the quality of his own process that he designed.

In addition to the odd role Mr. Aronoff is playing Your Honor will hear evidence that the trustees' review process was sufficient in many other ways. I'm going to explain the ways that the trustees' process was flawed based

on their own admissions.

First, there was no uniform set of policies and procedures provided to the five loan review firms retained by the trustees. Rather the loan review firms were left to their own devices, practices, and judgment to decide when there was a breach of a rep and warranty, and that's according to Mr. Aronoff.

Second --

THE COURT: Will there be actual evidence as to what they were told to do?

MR. COSENZA: To the extent that Mr. Aronoff testified to that, Your Honor, it's --

THE COURT: Okay. I guess that's wait and see.

MR. COSENZA: Yes.

THE COURT: Okay.

MR. COSENZA: Second, the initial quality control reviewers, the so-called QC-1 teams, this is a group of 12 to 15 individuals that did initial quality reviews of breach findings and claim submission packages, were directed not to review the actual loan files and probably did not even have access to them, because as Your Honor will hear, the QC-1 teams "weren't supposed to be poking around in the loan files."

Let's hear from Mr. Aronoff on this. Maybe we won't.

(Video deposition played)

MR. COSENZA: That raises real questions as to the efficacy of this quality control process, and Your Honor will hear testimony on that during this proceeding.

Third, a significant failure of the trustees' process relates to the trustees' failure to turn over to the plan administrator all third-party information they collected. This is really important, Your Honor.

For example, the trustees used third-party sources of information like the Bureau of Labor Statistics, which we'll refer to in this proceeding as BLS data, which I will discuss in more detail in a minute, and other third-party data.

The trustees used this data to purportedly prove that the borrowers made misrepresentations of one or more facts such as about their income or debt. But as Mr. Aronoff testified, the loan review firms did not turn over all third-party information to the plan administrator. The trustees only turned over information that was used to support a breach finding.

THE COURT: So let me draw down on this, because this was interesting to me when I read it in the opening brief.

So what you're saying is that there's third-party information, W-2s, tax returns, bankruptcy schedules, labor

statistics.

MR. COSENZA: Yes.

THE COURT: Okay. And what you're saying is that it's the plan administrator's position that the trustees during the protocol may have only provided, for example, a W-2 from two years after the loan administration that had one figure, but there may have been a tax return or a bankruptcy schedule that would support or -- that would support the plan administrator's position or undermine the trustees' position --

MR. COSENZA: Correct.

THE COURT: -- that was not submitted.

MR. COSENZA: That's correct, Your Honor.

THE COURT: Okay. And could you explain just at the level of preview --

MR. COSENZA: Yes.

THE COURT: -- how the Bureau of Labor Statistics' information would have been proffered or used in connection with establishing a DTI breach or another breach that was related to that?

MR. COSENZA: Sure.

THE COURT: That wasn't clear to me.

MR. COSENZA: So, Your Honor, you raise a very good point, I'm going to get to that literally in three minutes.

THE COURT: Okay. I will wait.

MR. COSENZA: So we will get to it.

THE COURT: All right.

MR. COSENZA: But that is an important point.

THE COURT: Okay.

MR. COSENZA: But in terms of -- again, the trustees only turned over information that was used to support a breach claim.

Now let's hear from Mr. Aronoff on this.

THE COURT: Okay.

(Video deposition played)

MR. COSENZA: Again, the question was whether the trustees included all of the third-party materials collected under loan review firms for a loan with their breach finding in the files transmitted to the plan administrator. Mr. Aronoff testified that those documents should not have been turned over to the plan administrator. This means that to the extent the trustees found information that could have refuted or contradicted alleged misrepresentations they likely did not turn them over to the plan administrator during the protocol.

Fourth -- now I'm going to get into more detail, I'm actually going to answer your question, Your Honor, now about BLS.

THE COURT: Okay.

MR. COSENZA: But it's coming.

THE COURT: All right.

MR. COSENZA: Fourth, the trustees relied on sources of information that were not designed to prove their claims.

Your Honor will hear from the plan administrator's expert on this point, but the three examples are BLS data, which I just mentioned, MIRS, and Accurint.

While sources such as these can sometimes be evaluated within the totality of the loan file the trustees' reliance on the data here was inappropriate.

As I just mentioned BLS data is a statistical survey that gives general estimates of income for certain categories of jobs in a given metropolitan area.

To support some of their misrepresentation of income claims the trustees compared the borrower's stated income at origination to the "90th percentile estimate in the BLS data." But Your Honor will hear testimony from Mr. Grice that BLS was never designed for this purpose and is therefore not a fully reliable source.

THE COURT: Can --

MR. COSENZA: Some of the problems --

THE COURT: So can I just --

MR. COSENZA: Yeah.

THE COURT: -- interrupt you again? So I'm trying

to understand this.

So somebody might put down on a loan application that they're a letter carrier.

MR. COSENZA: That's correct.

THE COURT: Right? And might put down a number for their -- is it their wages as a letter carrier or is it their income?

MR. COSENZA: It's supposed to -- I think it's supposed to be their income.

THE COURT: Okay. So their wages as a letter carrier might hypothetically be supplemented by working a night shift at a convenient store.

MR. COSENZA: That's correct.

THE COURT: Or might be supplemented by rent that they receive by renting out the basement apartment in their two-family home.

MR. COSENZA: That's correct. As a son -- I was the son of the captain of the fire department I can tell you about numerous of my dad's friends on the fire department who had second jobs, so it's just simply looking at what they received.

THE COURT: Okay.

MR. COSENZA: Yeah.

THE COURT: I'm just trying to --

MR. COSENZA: Yeah.

THE COURT: -- structurally understand --

MR. COSENZA: You're right on it, Your Honor.

THE COURT: -- the point, right?

MR. COSENZA: The point is it's just simply, you know, you don't look at all those other, you know, these other potential sources of income when you're using BLS data, it's just stating what the average --

THE COURT: What that occupation --

MR. COSENZA: Yes.

THE COURT: -- statistically in a particular --

MR. COSENZA: Yeah.

THE COURT: -- metropolitan area --

MR. COSENZA: Yeah.

THE COURT: -- without regarding also I guess to the particular seniority of the person --

MR. COSENZA: Yeah. That's correct.

THE COURT: -- involved and those kinds of factors. Okay.

MR. COSENZA: So, Your Honor, I can even put a finer point on this. Let me list some of the problems with BLS data.

THE COURT: Okay.

MR. COSENZA: BLS data excludes significant categories of compensation like overtime pay. BLS doesn't capture employee experience or specific job

responsibilities. BLS is prone to user error because it depends on the trustees' unidentified loan reviewers to select the borrower's right occupation. And most importantly, BLS does not establish with any given -- what any given borrower in this case earned at the time of origination.

The trustees -- now I will next move on to MIRS, which is another form of information the trustees relied on. They used that source to prove that borrowers misrepresented their debt obligations under applications by showing that they had undisclosed mortgages. But MIRS was never intended for this purpose and is therefore not a reliable source.

Here is the disclaimer that MIRS provided to its subscribers about its intended use.

THE COURT: You might be the only person ever to pronounce it mirrors.

MR. COSENZA: I know that. I've been criticized by many of my own team.

(Laughter)

THE COURT: Okay. The world at large refers to it as MIRS.

MR. COSENZA: MIRS.

THE COURT: All right? If the other pronunciation is hard-wired into your brain --

MR. COSENZA: Yes.

THE COURT: -- I'll accept it. But for anyone listening I think that Mr. Cosenza is talking about MIRS.

MR. COSENZA: Yes.

So it was not intended to be used in this manner, and the trustees -- if you look at this, Your Honor -- it says the companies do not verify the accuracy of information under link or system, nor do the companies warrant their reliability of any information retrieved. So it was not intended to be used in the manner the trustees did to prove that borrowers misrepresented their debt obligations on their mortgage applications.

Next, Your Honor, the trustees similarly relied on Accurint, and I can pronounce that one, an online search of public records to find borrower's addresses to try to prove misrepresentation of occupancy claims.

THE COURT: So can you tell me more about this database? What is it? How does it work?

MR. COSENZA: It's some method to show -- it's on online method to show how people or an individual is associated with a particular property or address. So you basically want to search a person's name, any address that the person would have been associated to, basically -- Your Honor, I'm looking at the actual --

THE COURT: Based on credit records, voting records, driver's license --

MR. COSENZA: Yes, some --

THE COURT: -- anything like that.

MR. COSENZA: -- cell phones is another one. Based on a cell phone applications.

THE COURT: Okay.

MR. COSENZA: So it's like all sorts of databases where this pulls from to try to associate --

THE COURT: And then Accurint comes to a, I'll use the word, conclusion as to what the person's primary address is?

MR. COSENZA: That's not my understanding, Your Honor. My understanding from looking at the files is it simply gives a list of the person's name and all the addresses associated with that person. So there's no, you know, conclusive link per se, but it just shows that that person somehow was associated with that address and it listed various addresses through --

THE COURT: Okay.

MR. COSENZA: -- keynote searches.

THE COURT: And how is it that you're saying that the trustees used this in connection with the occupancy breaches?

MR. COSENZA: So, for example, if I'm on a mortgage application and someone claims that they're going to use --

THE COURT: You're going to live in the home.

MR. COSENZA: -- this other home --

THE COURT: Right.

MR. COSENZA: -- they are use Accurint to show that during that same time period where the borrower indicated they should be living at that address, they instead were -- you know, their primary residence was at some other address based on what was listed on the Accurint data sheets.

THE COURT: So they would -- okay. I guess I'll just have to wait and hear --

MR. COSENZA: Yeah.

THE COURT: -- where the burden of proof. Because it sounds like what you're saying is that either Accurint or the trustees inferred that one address as opposed to another was the primary address.

MR. COSENZA: Based on -- yes, based on the various cells you see from the Accurint report they tried to --

THE COURT: Okay. All right.

MR. COSENZA: -- link between the properties.

THE COURT: Thank you.

MR. COSENZA: But, Your Honor, Accurint expressly states, "the system should not be relied upon as definitively accurate." Accurint admits that its data is

sometimes poorly processed and generally not free from defect. It cannot be used as the trustees used it here to definitively prove a misrepresentation of occupancy claim. And this is the Accurint disclaimer, Your Honor.

This is just true of a number of the various data sources used by the trustees. These data sources have to be analyzed in context. They do not establish (indiscernible - 57:33) facts to prove a breach of a representation of warranty.

Despite these material issues of reliability and contrary to the trustees' claim that the plan administrator disregarded such evidence, the plan administrator considered these sources and gave them appropriate weight in the context of all the facts and circumstances of each borrower's loan file.

Your Honor, another critical flaw in the trustees' process was that the trustees did not conduct an AMA -- as I mentioned earlier -- adverse material effect analysis separate from their breach analysis.

Your Honor, AMA means that a breach of a rep and warranty adversely materially effects the value of the loan for the interest of the certificate holders under relevant trust at the time the trustees made their claim.

The trustees' approach to submitting claims in the protocol almost completely ignored the provisions meaning,

reading it out of the contracts.

As Your Honor will hear from Mr. Aronoff the trustees did not conduct an individual assessment to determine AMA.

Let's hear from Mr. Aronoff.

(Video deposition played)

MR. COSENZA: So I will later --

THE COURT: Could you do some math for me on this?

MR. COSENZA: Yes.

THE COURT: So he's referring to a five percent threshold --

MR. COSENZA: Correct.

THE COURT: -- right? So that means that a borrower -- hypothetically a borrower represents income at $100,000.

MR. COSENZA: Okay.

THE COURT: And if the trustees find proof in their view that in fact the borrower at the time of origination only had income of $90,000 --

MR. COSENZA: Correct.

THE COURT: -- that would probably violate -- thres (sic) the 5 percent threshold --

MR. COSENZA: Correct.

THE COURT: -- and that without any further analysis the trustees' position is that that disparity

materially had an adverse material effect on the certificate holder's interest in the loan.

MR. COSENZA: That's correct, Your Honor. I will later in my presentation detail the (indiscernible - 1:00:02) responses the trustees provided in the protocol that they claim purportedly demonstrated AMA.

Next -- last what I will preview for Your Honor today has to do with --

THE COURT: Is there -- I'm sorry to keep interrupting you --

MR. COSENZA: No.

THE COURT: -- I'm just trying to --

MR. COSENZA: No worries.

THE COURT: -- fix this in my mind.

So is there going to be proof by the trustees, if you know, or argument by the plan administrator as to how the -- that category of breach claims sorts? In other words how many loans -- as to how many loans was it a 5 percent miss versus how many loans was it a 50 percent miss? Is there going to be data on that in the coming weeks?

MR. COSENZA: There may be from the trustees, I guess we'll have to wait and see.

THE COURT: Okay.

MR. COSENZA: Your Honor, the last flaw I'm going to preview today has to do with the trustees' submission of

missing document claims, which represents about 20 percent of the claims still at issue here.

The evidence will show that the trustees typically based their claim on the document being missing at the time the trustees reviewed the files during the protocol, usually 7 to 14 years after the loan originated, but the trustee seemingly ignored other evidence in a loan file that indicated the missing document was there at origination.

For example, some of the files contained evidence such as a contemporaneous checklist that indicated that the particular document was in the file at origination.

The evidence will show that the trustees failed to prove the chain of custody for the loan files, which courts have found necessary to prove a missing document claim.

Your Honor will hear from Mr. Grice about why proof of chain of custody is critical.

Well, Your Honor, we've put together a little graphic to demonstrate, you know, the problem with the trustees' theory.

The loans at issue originated between 2012 -- sorry -- 2002 and 2008. The trustees sat idle through many years and did not collect the loan files until 2015 and 2016. During those many years when the trustees elected not to pursue their claims the loan files changed hands many, many times.

I'm going to provide now a very, very simplified description of what happened to these loans after they originated, which is illustrated by this graphic. And Mr. Grice is going to testify to this in more detail, Your Honor.

After a loan was approved by the originator the closing agent's copy of the file moved to the subsequent loan purchaser. Then the file was sent to a sponsor like Lehman Brothers that securitized the loan. Eventually the loan file made its way to the master servicer or servicers where a hard copy version of the documents were likely removed from their file folders and then scanned.

It is important to note that in the protocol the trustees only made their requests for the loan files from the last servicer of the files. Those are the only files that the trustees collected. The trustees have not attempted to prove that the files provided by those servicers contained the original contents of the files as of origination, and there are obviously many documents in these files moving to various places over time.

Your Honor will hear that documents missing from the file in 2015 and 2016 very well may not have been missed at origination, as I mentioned earlier.

Your Honor will hear that simply put there is no chain of custody here, and there's no evidence as to what

happened to missing documents in the loan files. Were they missing originally? Would they go missing the 7 to 14 years post origination before --

THE COURT: So somebody on the second or third hand off could have decided that an appraisal was too big to copy.

MR. COSENZA: Or spilled coffee on the file or somehow when it got scanned a page went missing.

THE COURT: And remind me what I read about any indications as to whether or not a particular loan file was digitized at a certain point in time. It may -- I mean certainly --

MR. COSENZA: Yeah.

THE COURT: -- we're back to 2002, it seems unlikely that folks were digitizing things --

MR. COSENZA: That's correct.

THE COURT: -- back then.

MR. COSENZA: That's correct, Your Honor. And we'll explain this more during Mr. Grice's testimony, but there were a number of the files that were digitized. I can't give you a percentage as to what it was, but I think it's at least over a third, if not more.

THE COURT: Okay.

MR. COSENZA: Despite the expert testimony Your Honor will hear regarding the loan files movement and

deterioration over time the trustees initially asserted approximately 74,566 missing document claims. These types of claims flooded the protocol and created an enormous burden on the plan administrator as we were trying to respond to the claims put forward by the trustees in step one of the protocol.

Indeed Your Honor will hear that the plan administrator even located many of the allegedly missing documents during step two of the protocol. While it was very challenging, Your Honor, we tried to do it. And, Your Honor, the trustees' dropped about 52,000 missing document claims before they submitted their expert reports in this proceeding.

As Your Honor knows the trustees failed to provide an explanation for why they dropped those claims and cloaked the decision in attorney/client privilege, as I mentioned earlier. But it's hard to understand why they still decided to pursue the 18,540 missing documents claims here that remain in the case today given the faulty chain of custody and weak evidence for these claims.

Further, Your Honor will hear that the trustees made the strategic decision only to collect documents from the last servicer and not from anyone else.

Indeed Your Honor will hear from Mr. Edmond Esses, who worked at Duff Phelps. Mr. Esses was responsible for

collecting loan files from the servicers.

Let's hear what Mr. Esses testified to about the trustees -- about the efforts the trustees made to collect files before asserting almost 75,000 missing document claims.

(Video deposition played)

MR. COSENZA: This is significant, Your Honor. As Mr. Esses testified, the trustees did not even consider any other sources for missing documents besides the loans last servicers. This is striking given the intent of the protocol and the Court's clear availability to assist the trustees with their efforts to collect documents.

So the trustees elected not the establish a valid chain of custody or do any additional work in collecting loan files from other sources. Instead they made the strategic decision to flood the protocol with these claims. A large number, Your Honor, that really burdened the protocol and then later withdrew a large past of this -- of those claims during this estimation proceeding. For those reasons all missing documents claims should be estimated at zero.

Next, Your Honor, we'll hear testimony from the plan administrator's review of the loan files that confirmed what we told the Court in December 2014 when we moved to the entry of the protocol order was correct. Namely that every

loan needs to be reviewed holistically, because each loan has unique characteristics and requires an individual analyze. Indeed, Your Honor, each loan file is like a snow flake.

In all seriousness, Your Honor, you will see that these loan files are incredibly complicated and each one tells a different story and is unique. In essence each file represents a fragmented snapshot of the borrower's financial life.

Your Honor will hear testimony that the trustees' and plan administrator's witnesses agree that each loan file is unique. When the trustees' expert, Mr. Driscoll was asked to make a generalized assessment about whether misstatement of income of six percent would be material he testified:

(Video deposition played)

MR. COSENZA: So the parties are in agreement on this important point, which should come as no surprise. Despite the parties' agreement on the uniqueness of each loan file Your Honor will hear that instead of reviewing files holistically the trustees reviewed them myopically. The trustees tired only to find evidence that would support a breach finding and they ignored contradictory evidence in the file. I'll describe one particular loan file as an example for Your Honor. This is loan ending in 8999.

The trustees asserted a breach based on alleged misrepresentation of employment. The borrower stated on his application, dated April 11, 2007 that he was employed as a pastor. Your Honor will hear that the pastor's employment was verified when he applied -- this is back in 2007 -- through an origination verification of employment. This is often referred to as a VEO. So this is a contemporaneous VOE, Your Honor, from 2007.

The trustees here claim however that the pastor misrepresented that employment. What did the trustees rely on to make that claim? The trustees rely on a phone call made by a forensic analyst in 2015 to a bookkeeper at the pastor's church, a call made eight years after the loan was issued. The bookkeeper allegedly told the forensic analyst that the pastor's employment ended approximately March 15, 2007, which is a month before the loan closed.

Just to be clear, despite having a verification of employment obtained at origination the trustees elected to obtain another verification of employment eight years later and they fully credit that VOE discrediting the one that was already in the file.

This is just one example of the trustees' flawed process, which is structured to maximize the number of claims put through the protocol.

I will not be spending much time on the specifics

of each loan file in my opening, Your Honor, because as I said, they're quite unique and difficult to walk through, but Your Honor will hear evidence from Mr. Trumpp, Mr. Grice, and Mr. Castro on particular loan files to illustrate several different points about the trustees' flawed loan review process.

As Your Honor knows from the trustees' brief the trustees claim to be shifting their focus on the "big four breaches." Income, debt, occupancy, and excessive debt to income ratio.

As I mentioned earlier, it is our understanding that the trustees intend to prove their $11.4 billion in claims by focusing on these breach types and proving that the types of evidence the trustees submitted in the protocol to support them are used in the industry. But as Your Honor will hear saying that the types of proof the trustees relied on could be accepted in the industry does not mean that the trustees proved a particular breach on a particular loan. The trustees again conflate relevance with sufficiency. This is a critical issue, Your Honor, and a pervasive problem with the trustees' approach throughout the protocol.

Among other problems that Mr. Grice will testify about, one overarching theme is the trustees systemically credited any one piece of evidence in the loan file often obtained many years after origination like the pastor's loan

file we just discussed over the borrower's contemporaneous statements on that loan application as well as the information shared with the loan officer.

Although the Court is aware of much of this I want to provide some background on the loan origination process to put the trustees' claims into context.

Again, almost all the loans originated between 2003 and 2007. The process typically began with the borrower meeting with a loan officer to secure a mortgage to buy a home. The borrower's occupations span a very broad range of job types and there are different facts and circumstances surrounding each borrower's need for a mortgage. There are typically many interactions between the borrower and loan officer before the decision was made to issue the loan.

The trustees' disregard that the loan officer was closer to the borrower and particular facts of the loan as compared to the trustees' loan reviewers who were looking at the file many years later, in some cases a decade or more, after origination. But the trustees are now trying to move forward on their big four claim types without any specific proof of intent arguing that these misrepresentations by borrowers were intentional across the board.

The plan administrator acknowledges that a number of borrowers made misrepresentations on their mortgage

applications. We are sure that Your Honor will hear about some of those borrowers during this hearing, and in fact the plan administrator has accepted many of the breach claims put forward by the trustees, but the trustees are trying to do something different here, Your Honor, they're trying to have the Court assume that all of these borrowers made intentional misrepresentations to support 70,000 misrepresentation claims.

Your Honor will not hear any evidence of any borrowers at this point or from any loan officers. Your Honor will certainty not hear sufficient proof to find that tens of thousands of borrowers made intentional misrepresentations on their loan applications.

The trustees have been steadfastly trying to avoid sustaining their burden of proof on these claims. Instead the trustees maintain that based on inference and argument the trustees have met their burden on all of these misrepresentation claims. Your Honor, we've been hearing at that for years, since 2009, without the trustees providing sufficient proof, but the time for inference and argument has passed. And as Your Honor will hear, many of those borrowers were gainfully employed individuals who took out a mortgage and may not have been able to make their mortgage payments due to life circumstances. And Your Honor will hear that the trustees have asserted claims with respect to

more than 10,000 loans that are current today. That means the borrowers are still making payments on those loans. In fact the trustees' expert, Mr. Morrow testified that in his experience most borrowers do not lie.

The trustees' position -- I'll give you context for his testimony that we're going to play now -- the trustees' position as stated in their pretrial brief is that the borrower's failure to disclose debt that closed after the loan origination violates representations in the governing agreements, but when Mr. Morrow was asked whether as a banker he had ever sued a borrower for failure to disclose debt that was planned but not yet undertaken at the time of origination he could only remember one instance. Instead he testified that clients or borrowers are most of the time honest.

Let's here from Mr. Morrow.

(Video deposition played)

MR. COSENZA: And that's it from Mr. Morrow, one of the trustees' experts, it's his view that most of the time borrowers do not lie or make misrepresentations.

Your Honor will hear about other problems with the trustees' process and claims. According to the trustees their only burden is to prove a breach of a representation or warranty, if they make that showing for a given loan the trustees' theory is that they are entitled to be compensated

for all losses on that loan in the form of the full contractual purchase price as they calculate it, including speculative future losses and unrecoverable interest. This is regardless of whether the alleged breach they proved had anything to do with the losses.

The trustees' approach is flawed in at least three fundamental respects.

First the trustees' contractual AMA analysis is wrong. In their view, as I mentioned to Your Honor earlier, material breach necessarily adversely materially affects the value of the loan. The evidence will show this approach to AMA cannot with reconciled with the language of the contract and that the trustees' approach reads AMA out of the contract. The AMA language requires an additional individualized explanation of how a particular loan breach adversely and materially affects the value of the loan at the time the breach claim is made.

The trustees' failure to do this analysis left their claims devoid of a necessary aspect of their proof, yet the plan administrator gave credit for the existence of AMA when we independently saw it existed in a particular file. And this fundamental disagreement about the burden imposed by this requirement is one of the key reasons why the protocol process ultimately stalled.

Second, the trustees wrongfully demand breach of

contract damages without proof of a nexus or relationship between the alleged breach and the entitlement to collect damages.

If there's one point that the parties agree on, Your Honor, is that the trustees did not attempt to make any showing that the asserted breach has a casual connection or nexus to the claim losses even though the trustee stated in the first line of their pretrial brief that this is, as I mentioned earlier "a straightforward breach of contract case."

The trustees are adamant --

THE COURT: Isn't the trustees' position that nothing in the governing loan documents requires causation? That's their point, right?

MR. COSENZA: That is their point, yes.

THE COURT: And your point is that because -- even though there may not be anything per se in the loan documents that uses the word causation, you're saying that we need to layer over this case first year contract --

MR. COSENZA: Correct.

THE COURT: -- law.

MR. COSENZA: That's correct, Your Honor.

THE COURT: Right. Breach, causation --

MR. COSENZA: Yes.

THE COURT: -- damages equals claim.

MR. COSENZA: Yes. And we discuss this in our brief. We had our Second Circuit case, this is not a disputed issue of law that you have to prove proximate causation for damages, and that's the Sterling National Bank case from the Second Circuit that we've cited.

THE COURT: Okay.

MR. COSENZA: So if the Court agrees that the trustees are required to make some showing of a nexus the trustees are entirely without proof on this issue, which affects each and every loan in their protocol. This could support estimating the trustees' claim at a level well below $2.3 billion in and of itself.

The third way that the trustees' claims are overreaching is how they're asking the Court to award damages.

First, the evidence will show that the trustees' calculation of their damages includes billions of dollars of interest that is subject to disallowance under 502(b)(2) of the Bankruptcy Code.

Second, some 20 percent of the loans at issue -- and I'm going to detail these more later, Your Honor. Second, some of the 20 percent of the loans at issue are still active -- as I had mentioned before -- and a significant portion of them are still current. In our view it's extremely unlikely that the trustees are entitled to

any damages on the vast majority of loans that have been performing for ten years or more. Of course the trustees like to point out that a large number of these loans that are still performing were modified in some way. However, the fact remains that these loans are still performing and generating income streams for the RNBS trust.

THE COURT: So let me stop you on that point. So you stated at the outset that this isn't a repurchase case, it's a damages case, right?

MR. COSENZA: That's correct, Your Honor.

THE COURT: So just trying to understand what the significant of that difference.

So in a particular loan where both sides would agree that there's a material breach but the borrower continues to pay ten years out, the trustees would take the position that they could put back that loan if Lehman were still in existence.

MR. COSENZA: That's correct.

THE COURT: Right?

THE COURT: And Lehman takes the position that with the loan still performing they wouldn't be able -- they wouldn't have a put-back claim?

MR. COSENZA: Your Honor --

THE COURT: Is that where it begins to make a difference that this is Lehman and not a live lender

anymore?

MR. COSENZA: So, Your Honor, this is improperly disclosed in one of their expert reports, but as the protocol process first started there was a discussion about Lehman taking in the active loans as part of a repurchase type approach and that was rejected by the trustees. They said that would be inequitable and they did not want that approach.

THE COURT: Oh, sure, I understand that.

MR. COSENZA: Yeah.

THE COURT: I'm not trying to -- that's not --

MR. COSENZA: Yes.

THE COURT: -- where I was going with the question. I'm just trying to understand what difference it would make if there were hypothetically an ability to put back a loan. And I think what -- I think what the trustees will argue, and they can tell me if this is not true -- is that notwithstanding that a loan continues to perform, if today they were to identify something that they believe is a material breach they would have a put-back claim. I think that what's their position is, right?

MR. COSENZA: Yes. And I think if we go to the second component of AMA and causation in order for them the quantify what the damages would be on that particular loan.

THE COURT: Got it. Okay.

MR. COSENZA: Your Honor, last point on active loans is that the trustees are asking the Court to estimate their damages on those loans based on a clearly flawed estimate of their current value, and we're going to discuss that later.

Lastly, even though this is a Court sitting in equity what the trustees fail to account for with their use of the purchase prices as a proxy for damages is the billions and billions of dollars in interest payment that the trusts have been collecting on these loans, including after Lehman's bankruptcy in 2008.

The trustees' purchase price calculations ignore these cash flows despite the enormous benefit that the trusts have received from them. That the trustees fail to take account of these cash flows in their brief and in their purchase price calculation is not equitable. I will discuss each of those flaws in more detail now.

First, on the trustees' not conducting an AMA analysis the evidence will show that the trustees did not conduct an AMA analysis required under the governing agreements and protocol order to prove a breach of contract.

Again, as we mentioned earlier, proving that a loan sold into a trust violated or breached a representation of warranty in the governing agreements is not sufficient to show breach of the governing contracts, which all have an

expressed additional requirement.

The second equally essential element of each of the breach of contract claims that the trustees must prove here is that the alleged breach adversely materially affects the value of the loan when the claim is made.

And, Your Honor, we put up a sample language from one of the MLSAAs, which shows that, you know, that the breach must adversely materially affect the value of the loan.

The evidence will show that the trustees elected not to do a proper AMA analysis for the claims they submitted in the protocol.

As I previewed for Your Honor before the trustees instead elected to provide generalized mechanical statements of AMA by breach type with no individualized showing of how each of the rep and warranty breaches they were asserting adversely and materially affects the value of the loans when the trustees' made their protocol submissions. The trustees had clear notice going to protocol that such evidence would be necessary to sustain their claim based on our 2014 protocol motion, the December 2014 hearing, and the protocol order itself, which requires the trustees to provide how a breach entitled them to a claim under the governing agreements and applicable law. Despite this clear notice the trustees elected not to do the work on AMA during the

protocol.

Your Honor will hear testimony that the appropriate standard in the industry for determining whether AMA exists is a finding that the breach one, led to a default, delinquency, or some other loss on the loan; or two, impeded the servicer's ability to enforce the terms of the loan in default.

Your Honor is going to hear from Mr. Dan Castro, an expert with other 30 years of experience, in the mortgage finance industry.

THE COURT: What were you just reading from?

MR. COSENZA: I think that's from Mr. --

THE COURT: Led to the delinquency. Where is that? Were you reading the standard or were you reading --

MR. COSENZA: Oh, no, I was reading from -- that's from Mr. Castro's report.

THE COURT: From his report.

MR. COSENZA: Yes.

THE COURT: Okay. All right. Mr. Cosenza, I'm looking at the clock, I'm looking at the page number. You folks have been sitting here for almost two hours. I think maybe we ought to take a five-minute break.

MR. COSENZA: Sure.

THE COURT: Okay? And then we'll come back. And to the extent that you go over the two hours either as a

result of my questions or otherwise, Mr. Shuster, do you have any objection to allowing Mr. Cosenza to finish, obviously with you being afforded additional time as well?

MR. SHUSTER: None whatsoever.

THE COURT: Okay. So why don't we take a --

MR. COSENZA: Sure.

THE COURT: -- we'll call it a ten-minute break because we'll call it a ten-minute break.

MR. COSENZA: Thank you, Your Honor.

THE COURT: All right? Thank you.

(Recessed at 11:27 a.m.; reconvened at 11:43 a.m.)

THE COURT: Please have a seat.

MR. COSENZA: Thank you, Your Honor.

THE COURT: Okay.

MR. COSENZA: So where we left off, Your Honor, I had mentioned Mr. Castro and his expertise, and he's evaluated numerous repurchase claims throughout his career. At this point, Mr. Castro will testify that to determine the presence of AMA, industry participants assess a multitude of factors, macro-economic factors, borrower factors, property factors, servicing factors, and loan factors, all of which affect the value of the loan.

He will testify to make a determination on AMA, one must review and consider the entire mix and weight of evidence in the loan file. Again, the evidence will show

that the trustees did not attempt to review the entirety of the loan file to determine whether their alleged breaches adversely and materially affected the value of the loans, whether their claim losses were caused by some external factors.

Indeed, Mr. Aronoff testified that for the AMA analysis, that the trustees undertook during the protocol, both the borrowers' payment history and servicing notes, which include various interactions between servicer and borrower and may have information on major life events, affecting the borrower, that are not relevant to the trustees' AMA analysis. Let's hear from Mr. Aronoff.

(Video deposition played)

MR. COSENZA: And even probably problematic is what the trustees did in the protocol to state how an alleged breach met their definition of AMA. The trustee simply gave the plan administrator these four stock statements. And we will call them out one-by-one, Your Honor.

The first stock answer is that the breach "increases the likelihood of default with respect to the loan, thereby increasing your credit risk associated with such loan. The breach causing an increase in credit risk is material and adverse to the value of the loan."

The second stock answer is that the breach

"increases the expected potential loss severity and likelihood of default with respect to the loan, thereby increasing the credit risk associated with such loan, a breach causing an increased credit risk is material and adverse to the value of the loan."

The third stock answer is that the breach "increases the potential loss severity and a likelihood of default with respect to the loan, thereby increasing the credit risk associated with such loan. A breach causing an increase in credit risk is material and adverse to the value of the loan."

And the fourth stock answer is that the breach "increases the potential loss severity with respect to the loan, thereby increasing the credit risk associated with such loan. A breach causing an increase in credit risk is material and adverse to the value of the loan."

Except for the deemed AMA claims, these are the four stock answers the trustees provided to show AMA for all the loans that remain at issue. These formulaic stock answers clearly are not sufficient to carry the trustees' burden here.

These responses provide no meaningful analysis of an individual finding AMA. Again, this is what the trustees believe carries their burden of showing AMA here in this case for each of their loans. Simply put, these responses

fail to do so.

Moreover, as we can see in red here, these stock responses are caveated in terms of "potential or likelihood of a loss occurring." Having failed to ground their claims on quote actual losses, the trustees' position creates the potential for an enormous windfall. The trustee has accused the plan administrator of providing similar stock responses to the trustees' claims, but that is not a proper comparison.

THE COURT: So before you move off of this slide --

MR. COSENZA: Yes.

THE COURT: -- I think that this is related, part -- in part to some of the Monoline cases, right?

MR. COSENZA: That's correct, Your Honor.

THE COURT: And is it the plan administrator's position that while this might work in a Monoline case, it shouldn't work here?

MR. COSENZA: That's correct, Your Honor. And even in the Monoline cases, you can look at Judge Rakoff's decision in those cases. There's still an element there where he says there has to be some level of proof of a proximate cause between the breach and the actual loss that the parties were attempting to recover, even in the Monoline cases, which are under an entirely different standard.

So, Your Honor, this is what we had, this is what we received in the protocol. And with the burden of proof on this issue, you know, it's the plan administrator's position that the trustees must do more than give stop positions to prove their claims.

As I discussed generally before, what the trustees are trying to do here simply is show that the presence of a breach increases the risk of loss on a loan, and that adversely materially affects the loan's value.

As Your Honor will hear from Mr. Castro, this approach is inconsistent with industry custom and practice and improperly conflates the breach and AMA determinations. Mr. Castro will testify that even if the risk of loss was the appropriate standard, the trustees did nothing to measure the alleged increase and risk of loss on each loan.

Mr. Castro will testify that an analysis would be necessary, because to prove a claim the trustees have to show the effect of the breach was both adverse and material.

Your Honor, you'll -- here's another fundamental problem with the trustees' risk of loss approach to AMA, that is the trustees measure AMA at the time of loan securitization, rather and at the time the breach claim is made. That analysis is inconsistent with case law, and the language of the contracts, which as I've mentioned several times previously says affects in the presence tense, which

is at the time the trustees made their claim.

There's no evidence, however, that the trustees analyzed the presence of AMA at the time they submitted their claims. To justify this approach, Mr. Aronoff in his expert report had to expressly disagree with the recent decision of when AMA is measured issued by a District Court Judge in the Southern District of New York.

Here's what Mr. Aronoff had to say in his expert report:

"In my experience, AMA is assessed -- the AMA assessment is made as of the time the transaction closed. I understand in a recent case Judge Castell had suggested that materiality should be assessed at the time a demand to repurchase is made. That is not my understanding, and in my view, is not consistent with industry understanding."

To be clear as a finer point, there is no evidence in the record that the trustees analyzed the presence of AMA at the time they gave the notice of the alleged breach as required by the case law.

Indeed, it's clear from Mr. Aronoff that he simply disagrees with Judge Castell and filed what he believed to be the appropriate industry standard. And now as a result, there's yet another fundamental deficiency in the trustees' proof of AMA, given that the trustees never undertook the

correct analysis during the protocol.

THE COURT: So is it that the trustees through Mr. Aronoff or otherwise, make the -- do not make an AMA assessment, merely, in other words, jump to what I'll call a deemed AMA, once you have material breach, or is it the case that it was done in your view as of the wrong moment in time? I thought --

MR. COSENZA: Your Honor, it's both.

THE COURT: It's both?

MR. COSENZA: It's both.

THE COURT: Or either.

MR. COSENZA: So you have one is that, they just get us to the stock responses and didn't do any analysis of AMA. Second is, even looking at those stock responses and what they claimed they did, they said they only did it as of the time of origination or securitization. They never did in the context of the time that they actually provided notice of their claim.

So there are two fundamental problems with how they undertook their AMA analysis. It all goes to proof, it all goes to what was submitted in the protocol. And our argument is, you know, each independently would warrant a finding that there's just a fundamental deficiency of proof and how they proceed in the protocol, and how they can try to prove up their claims in this proceeding.

As demonstrated by the trustees in their pretrial brief, it appears the trustees may attempt to rely very heavily on the statements made by LBHI and its affiliate employees in other repurchase litigation.

Your Honor, if the trustees try to introduce these statements as they did in their pretrial brief into evidence, there will be a series of evidentiary objections, and the trustees will need to provide a proper foundation for admission of these statements.

As Your Honor will hear, those statements are from different cases and are often quoted by the trustees selectively and out of context. They are also highly prejudicial to the plan administrator, and of little probative value for several reasons.

First, in many of those cases, LBHI and its affiliates were in the role of purchasers of whole loans, intending to sell them to upstream purchasers for securitizations. For whole loans, LBHI acted as a warehouse, and acquired the loans and then tried to securitize them.

If LBHI was unable to securitize a loan, due to a breach, it was clear the breach had a material and adverse effect on the value of the loan. As Mr. Castro will testify, the AMA analysis here is completely different and is much more nuanced. The securitized loans at issue here

have no trading value. To determine whether an alleged breach adversely and materially affects the loans in this context, one needs to analyze whether the breach affects the loan's value to certificate holders. Given this different context, the prior LBHI statements related to whole loans and do not correspond to the loans at issue.

Second, unlike many of the loans here, the loans from the prior LBHI cases they cite involve loans that often defaulted in a very short timeframe, following origination, including early payment defaults or EPDs. You'll hear from Mr. Trumpp on that point.

Third, as Your Honor has heard repeatedly, every loan is unique, and so too is the evidence necessary to prove a breach. So trying to extrapolate statements made about different types of loans at issue and LBHI's Downtian (ph) in cases to loans here is improper.

Fourth, the work done by LBHI to substantiate their claims in the Downtian cases was generally more substantial than the work done by the trustees here. Thus, LBHI's claims in those cases were based on a fuller record.

While the trustees likely argue that LBHI used the same types of evidence in the Dowtian cases as those used by the trustees here, again that assertion is incomplete. LBHI often conducted investigations of the facts and circumstances surrounding the loans, much more deeply before

pursuing claims.

For example, you'll hear from Mr. Trumpp, LBHI often contacted borrowers and loan officers to better understand their claims before pursuing them. Something that the trustees did not do in the protocol.

The next critical file will mention the trustees' failure to prove is the trustees' failure to prove a nexus between the breaches and the losses they claim.

THE COURT: Can -- let me ask you a question. So one example that I recall from reading the briefs is the trustees I believe take the position that in other cases, in other context, LBHI has said bankruptcy schedules trump borrower income statements.

MR. COSENZA: Yes.

THE COURT: Right?

MR. COSENZA: Correct.

THE COURT: And they point out I think that here you're taking the opposite approach.

MR. COSENZA: So, Your Honor, just two responses to that. One is, again every analysis of the loan file has to be read holistically, so our reliance on a bankruptcy file in that case, there would have to be, and we'll see from Mr. Trumpp, typically other supporting evidence in addition to bankruptcy filing, that would show what was made in origination was inaccurate.

THE COURT: So I guess my concern is that when we get to this inflexion points as you --

MR. COSENZA: Yes.

THE COURT: -- gave me the coming attraction --

MR. COSENZA: Yes.

THE COURT: -- that we're going to have these evidentiary issues, am I going to have actually drill down and make a determination as to what LBHI did or did not do in some other context? That sounds like --

MR. COSENZA: Yes.

THE COURT: -- a classic kind of trial within a trial that will be --

MR. COSENZA: Well we --

THE COURT: -- challenging.

MR. COSENZA: You know, we agree with you, Your Honor.

THE COURT: Okay.

MR. COSENZA: I think when you get statement-by-statement and see how it's being used, in order to assess whether there's a proper foundation, whether it's out of context, whether the parole evidence rule applies, so there's going to be a lot of, you know, we just have to sort of do it as it comes, and hopefully we'll get some, you know, guiding rulings from Your Honor about how to handle --

THE COURT: Okay.

MR. COSENZA: -- this going forward.

Your Honor, the next critical file I think I mentioned this later, is to prove that the trustees did not prove any nexus between the breaches and the losses they claim. The consequence of the trustees' flat application of the AMA provision is that the trustees' claim suffered from an incurable failure of proof. They have not provided any evidence to establish the necessary link between the alleged breaches and claim losses.

As I mentioned earlier, the trustees currently assert that the plan administrator is liable $11.4 billion of damages, based on breaches of reps and warranties for over 70,973 loans.

The trustees' position to protocol and in this proceeding, is that they're not required to prove the alleged breaches and any connection or nexus to a default or the losses suffered on the loans.

As I mentioned before, the trustees' position is that a proof of breach will significantly increase the risk of loss on the loan at the time it was securitized, they are entitled to recover all losses on the loan, in the amount of the full purchase price in the governing agreements.

The loan I'm about to describe to you is an example of why the trustees' view does not make any sense. This is loan ending in 5164 that the trustees asserted had a

misrepresentation of debt.

The loan was taken out by a couple from a small town in Massachusetts. They co-owned a local bakery and that was actually in New Hampshire for over 30 years. The loan closed in July 2005. The trustees allege that the couple did not disclose debt they acquired two months prior to the subject loan.

However, the couple went on to make timely payments on their loan for over seven years. And why did the payment eventually stop? Your Honor, as the wife explains in this hardship letter, her husband unfortunately passed away and she stated, that she could no longer afford to keep the property.

An astonishing revelation of the inappropriate nature of the trustees' approach, when the trustees asserted their claim on this file for misrepresentation, they did not even include the hardship letter in their claim file, which shows that the loss of the loan was not related to whatever breaches the trustees asserted. Yet, the trustees are still seeking the full purchase price of this loan as damages in this case.

As Your Honor can see from this example, the adoption of the trustees' position here that they can recover the full purchase price for every loan leads to absurd results and is particularly inappropriate in the

context of a bankruptcy, given the windfall that follows. It is also contrary to applicable law, as we describe in our pretrial brief.

THE COURT: In the Monoline case, though, right, assuming the facts are as you represented them, there would be a valid put-back claim, right? Because at the moment of origination, the issue would be stated one way, whether or not the loan would have been made.

MR. COSENZA: So, Your Honor, on this loan --

THE COURT: I know I keep going back to the Monoline cases --

MR. COSENZA: Yeah, I know, but in this loan, I think there actually wouldn't be a claim theoretically because the statute of limitation would knock it out.

THE COURT: Different issue.

MR. COSENZA: Right, that's a different issue.

THE COURT: Different issue.

MR. COSENZA: But theoretically using that the -- you're correct, that there would be -- there could theoretically be a recovery on this, assuming that there's some proximate cause between the breach and the loss that they would have met the -- you know, the breach requirement.

THE COURT: Yep.

MR. COSENZA: So, Your Honor, the trustees have a breach of contract claim under New York law, and they're not

bringing a repurchase claim. It's clear under New York law that trustees had to demonstrate a causal connection between the breach claims they asserted and the claim losses. Instead of doing that, the trustees did not take causation into account when presenting their claims. Instead, they claimed the burden of proof will satisfy by identifying the type of breach and asserting such breach by definition tends to increase the risk of loss on a loan. The trustees' breach claims then suffer from another fundamental failure of proof.

Your Honor, I want to mention another issue that the trustees' argument to the plan administrators quote 1 percent acceptance rate in the protocol is absurd, and this is from the trustees' brief. I just want to put that in context.

This assertion is misleading and irrelevant. This has nothing to do what the plan administrator is seeking here. But first, let me go through the math.

As Your Honor is aware as I mentioned earlier, the trustees flooded the protocol process with an unreasonable number of claims. Over 193,000 claims on 94,566 loans so we started with an inflated number of loans and a denominator of the trustees' equation.

Putting that problem with the premise of their math aside, the plan administrator actually found breaches

at a much higher percentage in this case than the trustees asserted in their brief.

First, as I will explain in more detail shortly, the plan administrator did not review approximately one-third of the loans at issue because of the trustees' failure to comply with the requirements of the protocol order.

There are approximately 30,000 loans which the trustees failed to comply with the order, and the plan administrator did not review those loans because of the trustees' failure. So those have to be removed from the denominator.

During steps two and three of the protocol, the trustees also rescinded loans, and there were a number of trusts that collapsed and loans that liquidated without a loss. So those have to be removed from the denominator as well.

In addition, as I mentioned several times, Your Honor is aware the trustees abandoned 15,107 loans before they submitted their expert reports.

So reducing the denominator to reflect the loans reviewed by the plan administrator during the protocol that may have compensable claims results in a much lower number, approximately 47,775 loans or half, roughly, that the trustees asserted in their brief.

Now, we have a proper denominator, even using the

inflated number of claims put forward by the trustees in the protocol.

Next, we will now move on to calculate the appropriate numerator. We start with the fact that the plan administrator approved 1,260 loans during the protocol process and subsequently this summer. In addition, the plan administrator, and this is important, agreed that there was a valid breach claim for another 3,000 or so claims, so that increases the numerator in this equation. However, for those 3,000 or so loans, the trustees failed to demonstrate AMA for reasons I just explained.

So even though the plan administrator agreed on the breach, we didn't approve that claim because there was no AMA to determine proper AMA foundation for that claim.

So the number of loans for which a plan administrator actually agreed that the trustees' breach findings is actually 4,339.

THE COURT: But now I'm getting confused.

MR. COSENZA: Yes.

THE COURT: Okay. Because I feel like I've got oranges and apples. In the denominator I've got loans, right.

MR. COSENZA: Yes.

THE COURT: And the numerator now, I thought I just heard you add loans and breach claims.

MR. COSENZA: I'm sorry.

THE COURT: Did I get that wrong?

MR. COSENZA: I may have misspoke, but these are loan totals, so I've not conflated the loan and breach claims. I may have said breach claims --

THE COURT: Yes.

MR. COSENZA: -- so we approved the breach claims for those 3,000 and so they were passed at that point, but they were not fully approved as a claim because they failed on the AMA issue.

So we have 1,200 or so loans, Your Honor, that have been approved by the plan administrator --

THE COURT: Right.

MR. COSENZA: -- both on breach and AMA, then you have another 3,000 --

THE COURT: Okay.

MR. COSENZA: -- that we approved on breach, but because there's no AMA analysis they sort of remain in limbo as part of this proceeding. So you have --

THE COURT: Okay. So this is supposed to depict as a percentage of the --

MR. COSENZA: Loans reviewed.

THE COURT: -- loans reviewed.

MR. COSENZA: That they can be compensated for, the number of loans that we agreed under breach

determination.

THE COURT: So stick with me for a minute.

MR. COSENZA: Sure, sure.

THE COURT: Because I'm still trying to decide if you can have -- if the numerator is breach claims, then why isn't the denominator breach claims? I just feel like it's a percentage with apples in the numerator and oranges in the denominator or vice versa. I get what you're saying --

MR. COSENZA: Yeah.

THE COURT: -- about the breach claim.

So you're saying that we approved -- we, the plan administrator --

MR. COSENZA: Agreed.

THE COURT: -- approved those breach claims --

MR. COSENZA: Yeah.

THE COURT: -- right? We don't get to AMA, but look at all these breach claims we agreed with.

MR. COSENZA: Yes.

THE COURT: Right? But then you're comparing a percentage -- a number of breach claims as a percentage of approved loan claims, and that's where it's a squirrely fraction in my mind.

MR. COSENZA: Sure, no, I understand, Your Honor. This is just intended to illustrate that on their breach level, as percentage of loans that we reviewed --

THE COURT: Breach level, okay.

MR. COSENZA: -- what we actually for the loans, how many we agreed on with the trustees.

THE COURT: All right.

MR. COSENZA: I understand your concerns. These are not -- the point is they're not approved loans and there's other complexities here.

THE COURT: Right. But I'm just trying to connect up what the trustees have said about breach. If they're characterizing it this way, then okay, I'm comparing --

MR. COSENZA: Yes.

THE COURT: -- two numbers represented -- that the representation of the number is what you're both talking about.

MR. COSENZA: Sure.

THE COURT: As opposed to breaches that you agreed with as a percentage of breaches that they asserted, which is many, many times larger.

MR. COSENZA: Yes, that's correct.

THE COURT: Because the denominator would be many, many times larger, right?

MR. COSENZA: That's correct, Your Honor.

THE COURT: Okay. I understand what you're saying.

MR. COSENZA: Okay. Doing the math that reflects

a 9.1 percent breach pass rate, which is an agreed rate nine times higher than what the trustees asserted in their brief.

But, Your Honor, this is actually the most important point of this analysis, and further evidence of the plan administrator's efforts to be fair in this proceeding, the assumptions that Dr. Cornell that you'll hear about during his testimony, used to generate a claim value in the $2.38 billion range that the plan administrator is seeking to estimate the claims, Professor Cornell on their big four the trustees rely on, he uses a breach agreement rate of over 40 percent on those claims. And that's -- reflects the $2.38 billion number they were seeking estimation on.

So any characterizations made -- the trustees make about the unfairness of our process in the breach pass rates do not hold water.

Now, I'm going to speak about the trustees' damages calculation. The trustees will offer testimony from Dr. Carl Snow on the alleged losses suffered by the trust. However, the evidence will show that the trustees have not met their burden to prove the quantum of damages they seek.

First, the trustees use the full purchase price to calculate their damages. The use of the full purchase price in this matter ignores the realities of the protocol.

As I mentioned earlier during this -- during my

presentation, that this estimation proceeding is intended in part to estimate what the protocol would have yielded if the parties completed steps three through five of the protocol process.

During steps three and four of the protocol, the parties were supposed to engage in business person-to-business person settlement discussions for each loan. And then if that failed, a mediation process for the parties to come to a compromise on the appropriate value for each loan.

As part of that process, the parties were supposed to evaluate the strengths and weaknesses of each breach claim, AMA, causation, and a sufficiency of the evidence put forward by the trustees during the protocol, in the context of each individual loan file.

Based on that analysis and the parties' discussions, the parties would work to reach an agreement about the value of the claims on each loan. However, here the trustees failed to account for steps three and four of the protocol and want a windfall with every loan at every issue by seeking the value of the full purchase price on all 70,973 loans at issue.

Your Honor, there are other fundamental problems with the trustees' assertion of the full purchase price. Here are the elements of the purchase price.

It reflects the unpaid principal balance of the

loan, unpaid and accrued interest at the applicable loan rate. And three, unreimbursed servicer advances.

Instead of breaking up these three components in his analysis, as he's required to do, Dr. Snow initially calculated the trustees' alleged damages, he testified that he did not disaggregate these three components. Rather --

THE COURT: So let me stop you there. So the first component, before we even get to the disaggregate. The unpaid principal balance of the mortgage loan as of when?

MR. COSENZA: As of after its liquidated or whatever, you know, after --

THE COURT: As of today?

MR. COSENZA: Well, I think it depends on the loan. So it's the unpaid principal balance of the mortgage loan would be post -- you know, after you take into account the liquidation proceeds, so the -- for a liquidated loan, it would be --

THE COURT: Right.

MR. COSENZA: -- once they actually experience the loss.

THE COURT: But how did they -- this is my confusion.

MR. COSENZA: Yes.

THE COURT: Did someone actually look to see what

the -- on a particular loan during a protocol, did anybody look at what the actual unpaid principal balance was?

MR. COSENZA: Yeah. So there's supposed to be a document, it's like a loss certification that actually --

THE COURT: Yeah.

MR. COSENZA: -- breaks down to some degree some of the losses, and there's also like servicing expense log, it also breaks down the expenses, so you can try to tie to, you know, the losses that the trustees were seeking here.

THE COURT: But is it based on simply an amortization schedule, or would it be based on reality?

MR. COSENZA: I think it would be based on reality.

THE COURT: Okay. Okay. So now you --

MR. COSENZA: But again, just to be clear, that's on the liquidated loans, not on the active loans.

THE COURT: Right.

MR. COSENZA: The active loans are in a different category.

THE COURT: Right, okay.

MR. COSENZA: So instead of breaking up these three components --

THE COURT: Hang on a second. This is the balancing test we have between air and noise so.

MR. COSENZA: Sure.

THE COURT: Okay. So you were making the point about failure to disaggregate.

MR. COSENZA: Yes. So Mr. -- Dr. Snow testified that he used a realized loss data from the sur-reserves, which includes all of these elements combined less liquidation proceeds to get to the purchase price.

Particularly problematic for Dr. Snow's calculations that leads to the $11.4 billion in damages is that the date he relied on includes interest components that are not recoverable against a plan administrator in bankruptcy.

As the Court is aware, Section 502 of the Bankruptcy Code directs that claims be allowed as of the commencement date in U.S. dollars. For interest that accrued post-petition, the trustees cannot recover for this amount because the trustees had not yet provided the contractually required notice, and accordingly the claim for interest was unmatured.

Section 502(b)(2) of the Bankruptcy Code expressly prohibits the allowance of "unmatured interest." Yet, Dr. Snow initially did not separate -- separately calculate the interest component of the trustees' claim, either on a prepetition or post-petition basis.

The plan administrator's calculations indicate that the unrecoverable interest component is at least $2

billion of the claimed $11.4 billion in damages here on the liquidated loans.

It appears from the analysis that we received from Dr. Snow on Thursday evening that the trustees' calculation of unrecoverable interest is similar, approximately $2 billion. We're still reviewing this, in light of the late production of this request, and considering whether or not Dr. Snow's calculations were correct and need for rebuttal.

Second, the trustees have alleged billions of dollars of damages on active loans that we talked about earlier, Your Honor. The trustees have submitted claims on almost 14,500 active loans that remain at issue, which is about 20 percent of the loans still in this case, and they've alleged several billion dollars in damages on these loans.

The trustees relied on Dr. Elson (ph) to provide an estimated market value for these active loans. Mr. Castro will testify that these active loans are typically not subject to damages claims, because they provide investors with the value they sought in the first place.

Indeed, the trustees have been getting some sense of free option on these active loans, by collecting cash flows in the former principal and substantial interest payments for many years.

Beyond that, the evidence will show the trustees

have not carried their burden to prove damages for this category of loans. The evidence will show that the calculation of alleged losses and active loans is based on an unreliable method used to calculate their value.

The Court will hear testimony that the model used Adco's Loan Kinetics must be continually tuned and back-fitted by adjusting the model's output of the magnitude and likelihood of losses to match recent data.

The Court will also hear evidence of the windfall the trustees seek by pursuing claims on active loans. Indeed about 1,366 loans in which the trustees previously made claims of approximately $416 million have liquidated without a loss. Had the plan administrator paid out those claims when the trustees put them through the protocol, the trustees would have received a windfall of nearly half a billion dollars at the expense of other creditors.

I'm now going to go through the category of loans I'd mentioned earlier, Your Honor, the loans the plan administrator put on hold during the protocol.

All these on hold loans are subject to the defenses I described earlier, but I'll explain why the plan administrator put them on hold, and why the claims on these loans should be disallowed and estimated at zero because of the trustees' failure to comply with the protocol order.

Your Honor will hear testimony that the trustees

did not submit critical documents for the plan administrator to evaluate the claims on these loans during the protocol. First, this is Your Honor's question highlighted as before, the loss certifications. I'm going to detail all these in a minute.

Second, the corporate expense logs. Third, servicing notes and fourth payment history. These are documents that any prudent servicer should have or could easily generate.

I will talk more about the significance of these documents in a minute. But to give some more background, Your Honor will hear that the trustees' WARN notice since at least 2005, that the plan administrator could not review claims submitted by the trustees in the protocol without these documents.

As I mentioned earlier, Your Honor made clear to the parties at the onset of the protocol process that the Court would be available to assist the trustees to gather the necessary documents.

Despite being on notice all this time, the trustees elected not to obtain these documents. Your Honor will hear that the protocol required the trustees to produce, to the extent available and applicable, 41 documents. But after negotiations, the plan administrator was reasonable. The plan administrator agreed to compromise

and review of claims filed submitted by trustee in the protocol, if that claim file consisted of four categories of documents I mentioned earlier.

Your Honor will hear testimony that these documents were critical to evaluate AMA, breach, causation and damages, often providing the only contemporaneous record of what happened between loan origination and default. It also provides on the evidence for the amount unpaid on the loan and other relevant factors.

Let me explain why each document is important. Loss certifications. This has a servicer's calculation of the final loss on the loan, including a breakdown of unpaid principal balance at the time of foreclosure or liquidation, any accrued interest that remains unpaid and servicing fees.

The document is necessary to validate the purchase price calculation proffered by the trustees.

Corporate expense log, again, it reflects amounts that the servicer or their agents, like attorneys or appraisers have incurred in servicing the loan. Again, this is necessary to validate the purchase price calculation.

Next, servicing notes. Your Honor, these are important obviously for AMA and causation issues, because they reflect the servicing history of the loan. They include summaries of interactions between servicer and borrower, and may contain information on major life events

affecting the borrower, and records of other actions taken by the servicer relating to that loan.

Again, critical for us for AMA and proximate cause, as well as you could go to the breach analysis, and then they also shed light on whether the alleged breach claim by the trustee is valid.

Last is the payment history. It's a ledger of each payment or transaction made related to a loan, including payments of principal and interest by the borrower. This is necessary for AMA history, it's also necessary to calculate damages and part of our proximate cause analysis.

The trustees did not provide these documents, and the reason is because Mr. Esses, who was responsible for among other things, collecting loan files from servicers said that he did not believe these documents were necessary despite the protocol order.

Mr. Esses testified that he knew the plan administrator wanted the critical documents, otherwise, we would put the loans on hold. Despite being on notice of this issue during the protocol process, the trustee sat idle and never sought judicial assistance.

As a result, over a year ago on August 30th, 2016 we filed a motion to disallow and expunge the claims on these loans, which was pending before the Court before the

parties entered into the settlement agreement.

In light of Your Honor's decision regarding the expungement of the transfer loan claims, which was affirmed by Judge McMahon, the consequence for not submitting complete claim files prior to the protocol deadline was the expungement and disallowance of those claims.

In our August 2016 motion, we requested the expungement and disallowance of the claims for the on hold files. Just to be clear, Your Honor, it's the plan administrator's position that the claims for the on hold files should be estimated at zero.

The evidence will show that the trustees failed to comply with the terms of the protocol and failed to provide sufficient proof to meet their burden on these claims. Again, the trustees took no action to gather the necessary documents for these loans, despite repeatedly being put on notice by the plan administrator.

THE COURT: So let me understand what you're saying, that -- to go back to where we started. If the primary purpose or the sole purpose of this exercise is to determine what number would have resulted from the protocol --

MR. COSENZA: Correct.

THE COURT: -- then what you're saying is that under the protocol, this population of loans would have

failed.

MR. COSENZA: That's correct, Your Honor.

THE COURT: So is that what I am -- is that a finding that I need to make, or now that we are in the world of a settlement, am I supposed to be looking at those loans, what I'll call on the merits notwithstanding the failure to do what was necessary under the protocol and putting aside the overarching issues having to do with exemplars, et cetera?

MR. COSENZA: Sure.

THE COURT: Do you understand that question?

MR. COSENZA: Yes. So I can take it in different pieces. So our view is these loans, if they're not entered to the settlement, would have not --

THE COURT: Would have failed.

MR. COSENZA: Would have failed and they would've been expunged.

THE COURT: And they would've been disallowed.

MR. COSENZA: They would've been disallowed. In the context of these -- this proceeding Your Honor I think can just consider the strength of our -- of the plan administrator's position that these loans would've been expunged based on your prior order, and the fact that it was upheld by Judge McMahon on these issues and the compliance necessary for the trustees to produce documents by a certain

point, otherwise, the claims would be expunged.

So I think it's our view that they should be out of their case because of the failure to comply. But I think for your purposes, just something to consider in the total mix as you're trying to estimate these claims.

THE COURT: Thank you.

MR. COSENZA: Okay. Your Honor, I've just highlighted many of the deficiencies in the trustees' process of submitting claims, as well as a number of fundamental deficiencies in the trustees' proof.

Again, as I said earlier, we're going to an adversarial process against the trustees, and they'd have to prove their claims loan-by-loan, pursuant to the protocol. It is the plan administrator's position that the trustees' claims, based on their approach to the protocol and the current evidence they've presented would be in the neighborhood of $300 million.

But as Your Honor just mentioned, the parties are now in the settlement context, following a 9019 hearing. The plan administrator is not seeking to be punitive here, based on the trustees' evidence and their conduct during the protocol. We are trying to be fair.

We believe that we are requesting appropriate value that the protocol would have yielded had the trustees properly pursued their claims.

The plan administrator is duty bound to ensure that the trustees did not receive a windfall at the expense of other creditors. This challenge is not unlike other situations where the plan administrator has had to confront the estimation of monumental complex claims.

Within the context of the largest bankruptcy filing in U.S. history, the plan administrator has again always tried to be fair. Lehman does not exist anymore. It is the plan administrator trying to distribute assets and do it equitably.

As the trustees' expert, Mr. Aronoff noted in his deposition this is "note a normal put-back case." This is an estimation hearing within the context of a settlement agreement. And there are equitable principles of bankruptcy in play here.

Here is Mr. Aronoff's testimony on this point.

(Video deposition played)

MR. COSENZA: So Mr. Aronoff testified, and it should come as no surprise, he did not know how the governing documents play out in bankruptcy court here. And Mr. Aronoff has testified that the purchase price proffered by the trustees may not be the appropriate remedy here, given that we are in bankruptcy and this is not a repurchase case.

Let's hear from Aronoff on the appropriate remedy.

(Video deposition played)

MR. COSENZA: So as Your Honor and as the parties seem to agree, it's now up to you to fashion the appropriate remedy in this unique and complex proceeding.

As the Court is aware, there have been a number of outside claims brought against Lehman during Lehman's bankruptcy. They were brought at an exaggerated level, like a twelve foot person.

The plan administrator has always tried its best to be fair and equitable with all counterparties. The plan administrator has achieved fair resolution across an enormous number and range of claims. One of the few claims that we haven't been able to resolve is the claim brought by the trustees that is the subject of these proceedings.

In fact, the plan administrator did reach a resolution in 2015 with the institutional investors to right-size this claim as that issue here, as we've discussed during this proceeding. But we couldn't get a settlement done, because the trustees wouldn't accept a settlement for enough trust at issue. And now the trustees' claim is exaggerated again and is now back up to $11.4 billion.

Your Honor, based on everything you will hear, it will be impractical to come to a conclusion on breach, AMA, damages and sufficiency of the proof for each of the 70,973 loans that are at issue. That is not the purpose of this

proceeding.

The purpose of this proceeding, which is in the context again of a settlement agreement is to estimate the claims based on what would have happened during the protocol and a fair level for all creditors.

Indeed as I mentioned earlier, there are four guideposts that support estimation at $2.3 billion or less and will now provide more detail on each one.

First, the amount is equivalent to the settlement I just referenced between the plan administrator and institutional investors negotiated in October 2015. The institutional investigators agreed to accept 2.44 billion for the covered and transfer loan claims. Now this claim is at $2.38 billion because of a collapsed trust and an opt out.

And Professional Fischel will testify about the significance of the institutional investor support.

MR. SHUSTER: Your Honor, I sincerely apologize to you and to Mr. Consenza. I gave Mr. Consenza notice of this at the break. A plan administrator entered into an agreement with the objecting investors in which they agreed to withdraw their objections, and the plan administrator agreed not to put into evidence the institutional investors views concerning this settlement, whether they considered it fair and reasonable.

So I'm invoking that agreement and objecting on that basis.

THE COURT: Objecting to what?

MR. SHUSTER: To any statements by counsel for the plan administrator concerning the institutional investors support for the settlement here or belief that 2.44 billion is the right number and is a fair number.

THE COURT: Okay.

MR. COSENZA: I can deal with this in a minute, Your Honor, if that would help.

THE COURT: Okay. I'm not accustomed of having to have an argument in the middle of an opening statement.

MR. SHUSTER: I apologize. I just thought we had to make the objection.

THE COURT: Okay. Mr. Cosenza, could -- my hearing was that you said there was a settlement.

MR. COSENZA: Yes, back in October of 2015.

THE COURT: Right. And I didn't hear you say anything about what they think today.

MR. COSENZA: That's correct, Your Honor.

THE COURT: So there's no -- then there's nothing to talk about at this moment.

MR. COSENZA: That's our view, Your Honor --

THE COURT: Okay?

MR. COSENZA: -- in the settlement agreement

there's an express carve-out to allow this into evidence in this settlement agreement.

THE COURT: Okay. All right. Well, to the extent that I'm not properly understanding this, Mr. Shuster, you can revisit it at a later point, but we're going to keep going. Okay? Go ahead, Mr. Consenza.

MR. COSENZA: Your Honor, the Court will hear that the institutional investors are holders of approximately $6 billion in certificates in 85 percent of the participating remaining trust.

As Professor Fischel will testify, the large economic state in the trust gives them a powerful incentive to advocate for the best possible outcome for the trust.

Again, as I mentioned earlier, these are 14 of the largest and most sophisticated investors in structured finance, including Goldman Sachs Asset Management, Black Rock Financial Management, AGON, PIMPCO, MetLife and LAMCO, in fact the Court will hear that these institutional investors own or manage a combined total of more than $10 trillion in assets.

As I said earlier, the institutional investors also have significant experience in settling these types of RMBS claims. In fact, these same trustees relied on these institutional investors and their counsel in settling several other global RMBS disputes. For instance, in the

JPMorgan matter, all the trustees here were parties to that settlement.

In Citigroup, three of the trustees here were parties to the settlement, and ResCap, U.S. Bank and Deutsche Bank were parties to that settlement. But in this case, the trustees refuse to accept the institutional investor's views back in October 2015.

As I mentioned previously, this is based on a purported expert report from 2016 that the trustees have steadfastly refused to disclose in this estimation proceeding. One wonders why the trustees have refused to produce that report.

As Professor Fischel will testify, the institutional investors are the parties with a real financial interest here, not the trustees. And the Court will hear that the institutional investors previously in support estimation of the claims at the $2.38 billion level.

Second, Professor Fischel will also testify to the reasonableness of estimation at $2.38 billion in relation to all other large global RMBS settlements. In fact, Professor Fischel will explain how he determined that $2.38 billion is at the high end of the range of these comparable settlements.

He will testify that he analyzed all of the other large global RMBS settlements, which were subject to Court

approval, and he determined how those amounts compared to the settlement amounts in this case.

Even if there are differences across the litigations, which one would expect, given the complexities of these cases and that no cases are identical, Professor Fischel determined that $2.38 billion was a generous recovery by comparing the percentage of expected lifetime losses incurred by the trust, that were then recovered in each settlement, which he calls the recovery ratio.

To the similar percentage that would be recovered under the plan administrator's proposal and the trustees' $11.4 billion claim.

Professor Fischel will testify that the comparable settlements had recovery ratios ranging from 6.9 to 13.2 percent. Professor Fischel will also testify that the plan administrator's proposed allowed claim is at the high end of the range of recovery ratios, and the trustees' proposed allowed claim is several orders of magnitude higher.

Professor Fischel will testify that the $2.38 billion amounts to a recovery ratio here of 11.2 percent. As you can see on this chart, this is substantially above the recovery ratios for JPMorgan, Citigroup and ResCap matters. It's in line with the Countrywide settlement and two points below the ratio for the settlement relating to Washington Mutual.

Professor Fischel will also testify that the trustees' proposal of $11.4 billion amounts to a recovery ratio of 55 percent, which is more than four times as high as the largest recovery rate implied by any of the other settlements examined.

The Court will hear that the trustees' expert, Mr. Finkel (ph) admitted that the recovery ratio of 11.2 percent is within the range of settlements obtained by trustees' counsel and other RMBS cases.

In particular, in Depolt (ph) 2007, 083 and Depolt 2007, 084, the trustees represented by their counsel here where it sued on behalf of all certificate holders, not just a single group. Nevertheless, even on the most favorable assumptions, the recovery ratio in those cases was 12.47 percent and 13 percent respectively.

As Your Honor can see, these recovery ratios agreed to by trustees' counsel are very similar to the plan administrator's proposed recovery rate of 11.2 percent. Remarkably, as the Court will hear, the trustees' counsel failed to provide their expert Mr. Finkel with these settlements and cases, the trustees' counsel have previously litigated.

THE COURT: So spoiler alert question, so what are the trustees going to tell me that justifies the difference between the previous settlements and the proposed allowed

claims?

MR. COSENZA: I can't speculate on -- I know for the ones --

THE COURT: Is there any -- have I read anything yet?

MR. COSENZA: I know for the ones that have been part of Mr. Finkel's report, I know they're from individual trusts, from a particular trustee using a certain type of loan, maybe they're going to make, you know, some distinction. I think they're going to also make some distinction that here there's been a loan review process, so somehow all these other settlements are of no probative value, which you have a long protocol and process. I'm just guessing --

THE COURT: Okay.

MR. COSENZA: -- I think those are the arguments.

THE COURT: But I haven't read anything --

MR. COSENZA: Yes.

THE COURT: -- on this, right?

MR. COSENZA: Yes, that's correct, Your Honor.

THE COURT: In the opening briefs or --

MR. COSENZA: That's correct.

THE COURT: Okay.

MR. COSENZA: Your Honor, as a follow-up, you're going to hear from Mr. Finkel, the trustees' expert, that

other cases selected by the trustees' counsel are somehow the appropriate benchmarks. However, those cases are wholly distinguishable and involve only certain groups of loans with an individual trust from 2007, an entirely different collateral, home equity loans.

These are not comparable to the other global RMBS settlements discussed and analyzed by Professor Fischel. As a result, the self-selected cases put forward by Mr. Finkel should be given little weight, and we show that during this hearing, and the global RMBS settlements examined by Professor Fischel should be given significant weight in this estimation proceeding.

Third, as I mentioned earlier, the Court will hear evidence that outside of the context of this litigation, the trustees have accepted equivalent evaluations for identical RMBS claims in connection with the sale of RMBS claims owned by terminated trusts.

Now, as Your Honor knows, we have these six trusts that terminated during the pendency of this estimation proceeding. They are listed here. And Your Honor has heard that the trustees believe their claims are worth $11.4 billion, based on the protocol output.

However, the trustees sold each and every one of these trust claims at the exact amount or less than what the trust's allocable share would have been using the $2.38

billion level, at which the plan administrator is seeking estimation here.

Let me provide you with more background on this process related to the terminated trust and explain this to you in more detail.

For these particular trusts, the master servicer exercises its quote/unquote finical option (ph). This is a right whereby the master servicer purchased all the trust's remaining assets. The assets include all active loans, regardless of whether or not they were in default and any other assets in the trust, like the RMBS claims that the trustee submitted under protocol for that particular trust.

The price for the loan process is easy to calculate, it's simply the unpaid principal balance on the subject loan files. However, the clean-up option requires a process whereby the servicer identifies an appraiser to evaluate the trustees', the trust damages claims. The trustee has the right and obligation to accept or reject the appraiser.

Thereafter, the appraiser is directed to come up with a fair price or value for the sale of the claim by the trustee to the servicer.

Your Honor, I'm going to go through this process for each of the trusts. Let's look at Sorum 2004-5 (ph). The trustees asserted $13.5 million worth of claims through

the protocol for this trust.

Again, this reflects what the trust, you know, based on the $11.4 billion output in the protocol, that's the amount that's attributable to this trust. Yet in the clean-up call, the claims were appraised for that trust at $1.49 million. And the trustees accepted the appraisal and sold their claims to the master servicer at that value.

Now, what is the value for this particular trust claim, based on a plan administrator's proposed estimation amount of $2.38 billion using the allocation proposed by the trustees as to what each trust should receive? It's $1.49 million.

After the first trust was appraised, the trustees had the right to reject the master services appraiser. Yet, even after this initial evaluation, the trustees gave their consent to use the same appraiser.

Now, let's go to Escasco 2003-17A (ph). The trustees asserted $1.2 million worth of claims through the protocol for this trust. Yet in the clean-up call, the claims were appraised for that trust at $558,000. Again, the trustees accepted the appraisal and sold their claims to the master servicer for that amount.

Now, what is the value for this particular trust claim, based on the plan administrator's proposed estimation amount of $2.38 billion based on the allocation proposed by

the trustees, it's $558,000.

We move on to Escasco 2004-15 trust. The trustees' asserted $3.3 million worth of claims to the protocol for that trust. Yet, in the clean-up call, the claims were appraised for that trust at $97,000. And the trustees again accepted that appraisal and sold their claims to the master servicer for that amount.

Now, what is the value for this particular trust claim, based on the plan administrator's proposed estimation amount of $2.38 billion using the allocation proposed by the trustees? It's $316,000.

This is significantly higher than what the trustees' claims were appraised for. So to put a finer point on this, had that trust had remained in this proceeding and the Court agreed to estimate the claims at the $2.38 billion, this trust would have received three times more than what the trustee sold this claim for.

Moving on to Escasco 2004-282 -- I'm sorry, 28C, the trustees asserted $7.8 million --

THE COURT: So just to pause on that last point, because it's the outlier on this chart, right?

MR. COSENZA: That's correct, Your Honor.

THE COURT: Okay. So that supports the concept that the plan administrator is being more than fair.

MR. COSENZA: That's correct, Your Honor. That's

correct.

For this trust, the trustees asserted $7.8 million worth of claims to the protocol. Again, this is based on, you know, the level of this $11.4 billion claim that the trustees are seeking here. Yet, in the clean-up call, the claims were appraised for that trust at roughly $1 million. And the trustees accepted that appraisal and sold their claims to the master servicer for that amount.

Now, what is the value for this particular trust claims, based on the plan administrator proposed estimation amount of $2.38 billion, based on the allocation proposed by the trustees? $1 million.

Same for Labs 2004-1 (ph), that trust. There the trustees asserted $2.6 million worth of claims to the protocol. Yet, in the clean-up call, the claims were appraised for that trust of almost $400,000. The trustees accepted the appraisal and sold their claims to the master servicer for that amount.

Now, what is the value for this particular trust claims, based on the plan administrator's estimation amount of $2.38 billion, based on the allocation proposed by the trustees? It's $400,000.

Your Honor, the same could be said for the last trust, Escasco 2003-28XS, they asserted $1.1 million worth of claims for the protocol, the claims were appraised in

that trust at $113,000, and the trustees accepted that appraisal and sold their claims to the master servicer for that amount. And I think we all can guess, except for the one outlier what the trust would have received under the plan administrator's proposed $2.38 billion estimation amount, it's the same amount $113,000.

Five times the trustees authorized the assessment of other claims value at precisely the level the plan administrator seeks here, and in one instance, significantly less. The fact that the trustees sold the trust claims at the exact same value or less is a strong indication that $2.38 billion is fair and reasonable. And to put a finer point on this, Your Honor, this value in the second column here of this chart is the price at which a willing seller sold an asset to a willing buyer. There's generally no better evidence of value than that, as stated by Judge Peck in the Iridium case.

The next --

THE COURT: Do you have that data for every trust? I'm sorry, I stated that incorrectly. Is this -- does this represent the entire dataset for this --

MR. COSENZA: For these six, they are six terminated trusts, that's correct.

THE COURT: Okay.

MR. COSENZA: There's actually one other trust,

Your Honor, but we can't understand who's speaking for that trust, there have actually been seven that are terminated.

THE COURT: Okay. But this dataset is complete?

MR. COSENZA: Yes, yes.

THE COURT: Okay.

MR. COSENZA: The next guidepost to demonstrate that estimation -- so I'm going to move off from the terminated trusts, and I'm going to move to the next guidepost, to demonstrate the estimation of $2.38 billion or less is appropriate and that's Dr. Cornell's work.

The plan administrator had Dr. Cornell calculate the amount of success the trustees would need to achieve on their breach claims to reach a claim value in the $2.38 billion range. And Your Honor will hear that Dr. Cornell even accepted for the purposes of his calculations all the trustees' purchase price, which as I mentioned earlier has several flaws, as those numbers are inflated.

Your Honor can see from this chart that the plan administrator told Dr. Cornell to assume that the trustees can succeed under big four breach claim findings 40 percent of the time, and that the trustees would satisfy the AMA element, either 50 or 15 percent of the time, depending on how many payments were made on these loans.

Using these generous assumptions -- sorry, using these generous assumptions on all the trustees' claims, Dr.

Cornell calculated that the trustees' recovery would fall in the range of 1.6 to $2.5 billion.

Your Honor will hear testimony from Dr. Cornell on this, but to provide a little bit more detail and context for this, Dr. Cornell grouped the trustees' claims into the categories listed here on category -- I'm sorry, on column one of this chart.

Again, Dr. Cornell was given the assumptions by the plan administrator about the percent success rate for each of the trustees' types of claims, that's the information that's in column 2.

For example, for loans with a trustees' claim of misrepresentations of income, Dr. Cornell was told to assume that 40 percent of them would pass the plan administrator's defenses on a breach claim.

Next, despite the trustees' failure to provide any particularized evidence of AMA, the plan administrator assumed for these loans that satisfied the breach element, and had paid for less than 18 months, the trustees could meet their AMA burden at a rate of 50 percent.

As we will discuss, the relationship between a breach --

THE COURT: 50 percent of the 40 percent.

MR. COSENZA: Correct. As we will discuss the relationship between a breach and a compensable loss lessens

as time goes on, so Dr. Cornell was told to assume that loans are paid per 18 months or more would meet AMA and a rate of 15 percent.

Dr. Cornell made such assumptions as he will testify for all the different claims provided by the trustees. Based on these generous assumptions and applying the trustees' inflated purchase price calculations, Dr. Cornell calculated the aggregate claim value under four scenarios. They are referenced on this chart.

First, he calculated a claim value without on hold loans and without active loans, so we just removed those two categories from the calculation. That resulted in a recovery for the trustees of $1.63 billion. Next, again he used the same assumptions in this chart, but he calculated a claim value without the on hold loans but then he included the active loans, and his calculation came on that scenario to $1.92 billion.

Next, again using the same assumptions, he calculated a claim value including the on-hold loans, but not the active loans, and his calculation came to $2.11 billion.

Lastly, he included all of the on-hold loans, all the active loans, and again he applied the generous assumptions on this chart from the plan administrator. His calculation came to $2.49 billion.

As I mentioned earlier, Section 502(b)(2) prohibits awarding a matured interest which all these scenarios include. So all these scenarios were before we got the breakdown on the interest issue.

Given the trustees' produced unmatured interest calculations on Thursday evening, we're still in the process of fully understanding the import of those and how they impact Dr. Cornell's scenarios.

But the plan administrator's initial estimate and based on an understanding of the claim values, all four of Dr. Cornell's estimation scenarios would be reduced somewhere in the neighborhood of 15 to 20 percent, to take into account a matured interest.

THE COURT: So by the time we get to this, and how is this going to be handled? How are we going to desegregate or understand how the inclusion of what you characterize as unmature interest affects these? Because what it does is kind of put a collar around -- well, it informs how I would view challenges to the assumption -- to the success assumptions.

MR. COSENZA: Correct.

THE COURT: Right?

MR. COSENZA: Correct.

THE COURT: So --

MR. COSENZA: So, Your Honor, I guess my best

answer for you is --

THE COURT: -- I mean --

MR. COSENZA: -- maybe we can discuss this after --

THE COURT: Just we'll wait and see.

MR. COSENZA: -- but I think the --

THE COURT: That's fair.

MR. COSENZA: -- what you were trying to understand how to deal with this.

THE COURT: Okay. Somebody add this to the list of things we need to talk about later.

MR. COSENZA: Yes. Your Honor, just to conclude on the Dr. Cornell analysis, we believe all these scenarios demonstrate again that the plan administrator's request to estimate the claim at $2.3 billion or less is fair and reasonable.

In conclusion, Your Honor, for all the reasons I've outlined above, the $11.4 billion the trustees seek to estimate their claims at is without support. As I have discussed in detail and Your Honor will see during this hearing, there were significant number of flaws in the trustees' process.

There is no evidence in the record the trustees conducted a proper AMA analysis. There is no evidence in the record the trustees demonstrated any nexus between

alleged breaches and loss.

There are significant issues with the trustees' damages calculations for both active and liquidated loans, and there is significant deficiencies with the claims the trustees put in their protocol that the plan administrator put on hold.

All these reasons indicate why the $11.4 billion the trustee seeks, which again reflects a full purchase price and the trustees meeting their burden for every one of the 70,973 loans at issue provides no basis for the estimation of these claims at $11.4 billion level.

On the other hand, the evidence at the hearing will show the plan administrator's metrics including the four guideposts on the chart, all support estimation at $2.38 billion. The institutional investors support for settlement at $2.44 billion in October 2015, the comparable RMBS settlements, that the trustees have accepted equivalent evaluations of identical RMBS claims, when selling claims owned by terminated trusts, and looking at the generous assumptions provided to Dr. Cornell and the resulting recoveries and Dr. Cornell's estimation scenarios.

All of these guideposts support estimation of the trustees' claims at $2.38 billion or less. The plan administrator therefore asks the Court that based on the evidence Your Honor will hear, and after considering the

equities of this case, Your Honor estimate and allow the trustees' claim at $2.38 billion.

Thank you, Your Honor.

THE COURT: All right. Thank you very much, Mr. Cosenza.

Okay. So it's ten minutes before 1. Mr. Shuster, your call, you're the one that has to speak after the lunch break.

MR. SHUSTER: An hour or so?

THE COURT: An hour. Why don't we do an hour. So we'll resume at ten minutes before 2, and we'll go to the end.

MR. COSENZA: Great, thank you, Your Honor.

THE COURT: You can obviously leave all of your things here.

MR. SHUSTER: Thank you.

THE COURT: Thank you.

(Recessed at 12:52 p.m.; reconvened at 1:55 p.m.)

THE COURT: Please, have a seat.

So the sun is swinging around. If anybody finds themselves uncomfortably in the sun, let us know and I can already see somebody did my favorite least thing to my curtains.

MR. SHUSTER: Not me.

THE COURT: Okay. We have somebody admitting

guilt back there. Are you ready, Mr. Shuster?

MR. SHUSTER: Yes, Your Honor. May I?

THE COURT: Please come up.

MR. SHUSTER: May it please the Court. Your Honor, I want to begin by telling the Court how grateful the trustees are for the opportunity to present these claims. They're grateful to the Court for all the time and effort the Court has put into these claims thus far and all the time and effort the Court is committed to putting in going forward.

THE COURT: Of course.

MR. SHUSTER: Your Honor, this hearing is about defective mortgages that Lehman sold to investors. The evidence will show that Lehman materially breached its representations and warranties for tens of thousands of loans that it securitized. Stated simply, Lehman sold investors riskier loans than they agreed to purchase.

The trustees are here on behalf of all investors in these trusts. The total aggregate amount of certificates is $23 billion. So there are investor groups that have appeared here to some degree, they hold in the aggregate $6 billion, there's a great silent majority out there holding another $17 billion in paper, and their interests are directly at stake in this estimation proceeding.

To prove the trustees' claims, Your Honor, we're

going to show that -- we'll walk the Court through the --

THE COURT: Can I just ask a question --

MR. SHUSTER: Yes.

THE COURT: -- and I -- perhaps I should have asked it of Mr. Cosenza, but this is the first time I'm hearing more of the numbers around that.

So I'm not hearing anything or considering anything, nor should I, with respect to how the paper has moved around, right?

MR. SHUSTER: Correct.

THE COURT: So the current holders, some of them might be original holders and some of them might be secondary or tertiary, so to speak holders.

MR. SHUSTER: Absolutely, yes, that's correct.

THE COURT: So we're just -- we're just talking about face, par, notional amount --

MR. SHUSTER: Correct, yes.

THE COURT: -- however you want to talk about it.

MR. SHUSTER: Yes.

THE COURT: Very good.

MR. SHUSTER: Thank you.

So to prove our claims, Your Honor, we'll walk the Court through the trustees' process and show that it did generate reliable evidence that proves Lehman's breaches. We'll show the Court that the evidence that the trustees'

have amassed is probative of breach and is largely unrebutted, that the trustees drew valid and reasonable inferences from that evidence, and that those inferences and the evidence prove a material breach.

Now, of course, we will not attempt to show that on a loan-by-loan basis, or we would be here until the end of time. But what we will attempt to do is we'll ask the -- Your Honor to make judgments about types of breaches that are common across groups of loans, and that's how we propose that the Court get to an estimation here.

So there are, in fact, common types of breaches proved with common types of evidence across large groups of loans. There are common disputes between the parties on those breaches, on those evidence types, and on those loans, and we think that those disputes can be resolved as to types of breaches and groups of loans.

THE COURT: So this is the fundamental thing that we keep coming back to again and again, and as I've told you before, and I'll keep saying it throughout the trial, you know, this might just be me, but your statement of what you're going to show sounds to be at odds with the countervailing statement that every loan file is unique.

So I am continuing to struggle with the every loan file is unique, a snowflake, whatever you want to call it, compared to common types of breaches and a -- I won't say a

sampling or an -- a methodology that includes extrapolating from something small to something larger that you will then tell me adds up to your claim. I'm genuinely having a hard time reconciling that. Okay?

MR. SHUSTER: Yes, I hear that. And I -- in the course of what I'm going to say, I hope I can put -- make that more concrete and show the Court why -- what we're proposing is practicable and reasonable.

THE COURT: Okay. So let me ask one or two follow-up questions.

MR. SHUSTER: Sure.

THE COURT: So if we weren't in a normal situation either where a claimant against Lehman filed a proof of claim, right, you have the burden of proof, no question about it --

MR. SHUSTER: Yes.

THE COURT: -- right?

MR. SHUSTER: Yes.

THE COURT: And if you submitted ten proofs of claim, you would have ten separate burdens of proof, right? So then you have the fact that there are so many loans, so many claims and the additional complexity of it's a settlement reflecting the fact that we're doing an estimation. Is that what makes this --

MR. SHUSTER: Well --

THE COURT: -- different from -- putting aside we would be here until the end of time issue.

MR. SHUSTER: Yes.

THE COURT: There's nothing that relieves a claimant of -- let me ask it as a question. Is there anything in the procedural posture of this case that relieves the trustees of the burden on a loan-by-loan basis to establish the amount of the claim you think ought to be allowed?

MR. SHUSTER: So I don't know that there is, but we're not asking to be relieved from that burden.

THE COURT: Okay.

MR. SHUSTER: And let me explain how and why. And actually -- and I'll walk through this in a very concrete way. But what the -- we have submitted actually summaries that summarize each and every breach claim on each and every loan.

Now, those summaries come in a couple of forms. There is a claims tracking spreadsheet that was maintained between the parties during the protocol process. So that comes into evidence actually under Exhibit G under Section 7 --

THE COURT: Right, that's the unwieldy big thing, right?

MR. SHUSTER: Okay. But it does provide --

THE COURT: But that's the document you're talking about.

MR. SHUSTER: Well, that's one document.

THE COURT: Okay.

MR. SHUSTER: Then there are two exhibits in the original Aronoff report, Exhibit 15 and Exhibit 4, which also summarize on a loan-by-loan and breach-by-breach basis every breach. And those in our view, are admissible under Federal Rule of Evidence 1006 and those summaries themselves constitute evidence of loan-by-loan breach.

So we strongly believe that we have developed and are providing loan-by-loan evidence of breach. And we've talked a lot about the protocol, and I think I've said it before, but I know I want to say it today.

As trial counsel for the trustees I'm delighted by the protocol, because we were made to go out and get loan-by-loan evidence of breach and that's what we did. The claims that we have today are much stronger than the claims than we had in say December 2014, before we went out and got all of the evidence of breach.

So we're actually -- we're not asking to be relieved of the burden of providing loan-by-loan and breach-by-breach evidence of breach. I think there's a practicality here which is that it's not humanly possible for the Court to go line-by-line through that thing and say

yea or nay.

THE COURT: Right. But in UBS --

MR. SHUSTER: But the proof has been provided.

THE COURT: In UBS, though, right?

MR. SHUSTER: Yes.

THE COURT: Just Castell he had one of these, right?

MR. SHUSTER: Yes.

THE COURT: And he went loan-by-loan and then he said, the next couple of thousands of these, go and talk to a special master.

MR. SHUSTER: Right.

THE COURT: So he did actually do loan-by-loan, right?

MR. SHUSTER: Well, he and the special master did. I have been monitoring that case actually for a client.

THE COURT: I have. I've just read the copy that you've put in my binder.

MR. SHUSTER: But I'm quite confident they got to the point that they were resolving claims on a category basis. And I think honestly when the protocol was urged upon the Court that the plan administrator said that claims could be resolved, but in categories and groups and types of breach. That's -- and they submitted among other things, an expert affidavit from Mr. Penot (ph) the head of RECAFCO who

said that explicitly. That was part of why the protocol was supposed to work, because the parties were going to get to a point where they had, you know, common disputes on types of breaches and groups of claims, and they would make an effort to resolve those one way or the other.

I don't think that's how it ended up quite working. We have probably a strong difference of opinion with the plan administrator as to why that was, but --

THE COURT: Okay.

MR. SHUSTER: So, yes. So, you know, we will ask the Court to look at types of breaches and common disputes across those types of breaches, and across groups of loans.

So, for example, if you have a loan where a tax return shows that the borrower misstated his or her income by 20 percent or more, say you have a tax return from the same calendar year as the loan was originated. We say that's good and sufficient evidence of breach. The plan administrator says it isn't.

You can -- the Court can resolve that issue, and on that basis I think estimate a subgroup of the claims, and that's how we would propose that the Court get an estimation. The same is true if you're using say a MIRS report to establish preclosing mortgage debt of the borrower. And the question is, is the evidence reliable, is there -- have the trustee shown a material and adverse

effect, is that type of breach or that breach of the type that constitutes a material and adverse effect on the value of the loan, and do Lehman's -- are Lehman's defenses persuasive.

So that's how we propose that the Court go about it. I would like to start off by walking through one individual loan just to illustrate. So now I'm going to operate the clicker. Here we go. Oh, yes, may Mr. DeMay approach --

THE COURT: Yes, of course.

MR. SHUSTER: -- and hand the Court a couple of binders and --

THE COURT: Thank you very much.

MR. SHUSTER: -- we have copies for our colleagues on the other side.

Okay. So here's a loan for a property on Nickerbocker Avenue in Patterson, New Jersey. The borrower is Yen ET (ph), we have redacted the borrower's surname for privacy purposes. Subject loan amount is $448,000, it's a primary residence, supposed to be a primary residence. The closing date is January 25th, 2007.

So here is the loan application where the borrower indicates, if you can see at the bottom there, that she is employed at St. Joseph Regional Medical Center. No, sorry, I've got to remember to do this. I'll try to remember.

As a radiology technician and clerk. And then if we go to the next page, you can see that the borrower represents her monthly income on the loan application at $9,542 and there's -- she actually identifies other income which borrowers are asked to do, when in fact, they do have a secondary source of income. There's the total number. So that's a monthly and then we annualize the number just to give a sense of the magnitude.

The -- we then have the borrower's individual tax return for the calendar year leading up to, so the loan was taken out in January '07. This is the tax return for '06, so it would show her income or tend to show her income for, you know, the months immediately prior to the loan, and then we have a W-2 for the year the loan was taken out.

THE COURT: When was the --

MR. SHUSTER: The loan was closed in January of '07. This tax return is for calendar '06.

THE COURT: Okay.

MR. SHUSTER: So it shows an aggregate income number, just a gross income of $21,796, which is monthly under $2,000 a month. Then we have a W-2 that shows that the -- for 2007 shows the same job, same borrower, and $23,000 in wages, which obviously is just under $2,000 a month.

There is additional evidence in the loan file, let

me just note, not that it's particularly dispositive one way or the other, but this information when we have tax return information, W-2's things like that, that's already in the loan file that we got, we didn't go out and get it, I'm not sure we would have been able to do that.

So there, if you look at then this -- the following chart, we've noted the 2006 tax return, the 2007 W-2, there's other borrower supplied information in the file for subsequent years that shows -- which I just, in the interest of time, I didn't make copies of here, but which shows a consistent story in terms of the borrower's level of monthly income and the borrower's occupation.

So this income misrepresentation finding went through multiple layers of review. The loan files were obtained by the servicer, went to Duff & Phelps. Duff & Phelps provide the loan files to the loan review firms with instructions. The loan review firms determined, verified the borrower information, determined whether or not there was a breach.

Where they found there was a breach, they assembled the evidence of breach, claim package, the loan file and passed that on to Duff & Phelps. Duff & Phelps performed two levels of QC. The first level was to determine whether the claim file had all the contents that it said it had, whether the breach description was accurate,

and whether all materials were there, and the second was to determine conclusively whether there was a material breach. And then where that determination was made, it went on to Lehman.

This is what was submitted to Lehman, the claims package, which contain the supporting documentation. The -- which would've been the relevant pages from the loan file, the loan application and whatever the tax returns and W-2s and other additional material, and then a breach narrative that would've identified the defect and then described the breach and the evidence supporting the breach.

It says here that there's alleged defect number two, misrepresentation of income, it happens on this loan that there was an alleged defect number one, which was the DTI calculation, a recalculation of the DTI.

So Lehman rejected the claim and its rejection of the claim, the responses that it provided here are representative certainly and we'll obviously be looking at these in considerably greater detail, but it says that the evidence is unreliable and insufficient because income stated in a non-origination year tax return does not prove origination income.

There's no reference here to the other evidence that's in the file, but for present purposes that's actually not my point, I just want to walk through how this all gets

up to the summaries.

So this is identified in the claims tracking spreadsheet, and then the breach and the description of the breach, and the supporting information is reflected in, as I mentioned, Exhibits 15 and 4 to the Aronoff report.

So then the question is or at least a question is, how can the Court be sure that the evidence is what we say it is. Leaving aside even the question of whether it's sort of sufficiently probative.

The evidence was presented to Lehman, together with a description of the claim, and the basis for the claim is mandated by the protocol order. It is summarized in the claims tracking spreadsheet. Those materials come into evidence under Exhibit G. It's summarized in Aronoff 15 and 4, which we submit come into evidence under Federal Rule of Evidence 1006, which allows for the admission of summaries, as proof of the underlying materials.

And for us, this is a very important point, point five, Lehman does not in the vast majority of cases, challenge whether our evidence says what we say it says, particularly for the borrower breaches. If we say there's a tax return in the file that says X, there's a W-2. They don't dispute that. What they dispute is the sufficiency of the evidence.

Mr. Cosenza drew a distinction between relevant

and sufficient evidence and it's the plan administrator's position that this evidence is not sufficient. But in terms of whether it's actually there, whether it says what we say it says, and whether it is what it purports to be, I don't think that is materially disputed between the parties.

THE COURT: Can you help me out here, going back to slide -- it's on page 11 headed "Lehman rejected the claim." When it says "debtor findings number 2" so the evidence does not support a breach of the no fraud representation.

MR. SHUSTER: Right.

THE COURT: So to your point, which I accept that they're not saying that the documents not forged, the underlying documents, is what Lehman is saying here that there's no -- the next paragraph down, the no fraud representation requires seller knowledge.

Can you help me out in terms of if this was a misrepresentation as to income, and you could through a crystal ball discern that there was no seller knowledge, what happens in that instance?

MR. SHUSTER: There -- the -- there's no seller knowledge requirement. So this is referred to by shorthand as the no fraud --

THE COURT: As the no fraud, right.

MR. SHUSTER: Right. But it's actually the no

untrue statement representation and I'm going to ask my colleagues --

THE COURT: Okay.

MR. SHUSTER: -- if they can pull that up.

THE COURT: Okay.

MR. SHUSTER: Let's -- we can take a look.

THE COURT: So even if this -- you could get beyond the hurdle on no fraud because no seller knowledge, right?

MR. SHUSTER: Right. So --

THE COURT: You would say that this -- the underlying facts would demonstrate another kind of breach.

MR. SHUSTER: Yes. So the -- this is 104(c)(5) typically of the applicable loan agreements, we've got it up on the screen now, chart 22. It -- what Lehman is referring to is the last sentence of sub 5 there. There are four independent representations in section five that the note and the mortgage are genuine, that everyone had the legal capacity to enter into it. Then there's a specific representation that the documents, instruments, and agreements submitted for loan underwriting contain no untrue statement of material fact or omitted to state a material fact.

That's what we're relying upon. What Lehman is relying up in saying you have to establish seller knowledge

is the fourth sentence. And they're saying that the fourth sentence states the standard even as to sentence three, and it's our position as a matter of straight forward contract interpretation that that's not the case.

THE COURT: Okay. Thank you.

MR. SHUSTER: Of course. So if we could then go back to chart 12, please. No. Let's go further to 13. 15. Yes. All right. 13.

So now we assert the breach has a material and adverse effect. That's what the trustee's asserted in the protocol. They made a determination that -- a breach finding that goes to a misrepresentation of income or debt or occupancy has a material and adverse effect on the value of the loan. We will have experts testify on the issue. Importantly for us, Lehman itself -- Lehman and Aurora both used the same standard in pursuing put-back claims. In fact, they used a more liberal standard than we use. I will come back to that. For present purposes, it's enough that we believe we establish that there's a material and adverse effect of the breach.

So there are certain general -- coming back to our proposed estimation methodology, as it were, there are certain general disputes that are illustrated by this example. Are tax returns sufficient to show a borrower's income and, frankly, we might have added W-2s and pay stubs

which are also in the file. But for simplicity sake, does the misstatement of income have a material and adverse effect and do the clients overcome Lehman's defenses -- the Lehman's defenses or knock us off the claim?

THE COURT: But is that -- on the second point, does the misstatement of income have a material adverse effect --

MR. SHUSTER: Yes.

THE COURT: Going back to something I asked this morning, are you telling me that this is, in effect, a deemed AMA if there's a misstatement above -- that breaches a certain threshold?

MR. SHUSTER: As a practical matter, that's what it amounts to, that when a loan -- when a borrower misrepresents his or her income or debt or occupancy -- well, occupancy --

THE COURT: On this -- right now, let's --

MR. SHUSTER: Yes.

THE COURT: That's a --

MR. SHUSTER: Income.

THE COURT: -- different kettle of fish.

MR. SHUSTER: Yeah. Income and --

THE COURT: So right now I'm just talking about income.

MR. SHUSTER: Income. When a borrower

misrepresents his or her income in a non-trivial way above a certain threshold, that misrepresentation has a material and adverse effect on the value of the loan.

THE COURT: But this is my issue. You're stating that as a principle.

MR. SHUSTER: Well, we have --

THE COURT: Right?

MR. SHUSTER: -- finding to that -- what we have are expert opinions --

THE COURT: Yeah.

MR. SHUSTER: -- saying that when a borrower misstates his income or his debt, that increases the risk of loss on the loan.

THE COURT: So but is that -- going behind that, though, is that because statistically, based on analyses that underwriters and loan originators and servicers have done, you can then track -- well, you can do a launch to and a study of the loans over their life and you can correlate higher default rates to -- and track them back to misstatements of income? Or, is that simply kind of FIA that, by definition, above a certain threshold, the position is taken that that increases the risks on the loan and therefore it's a deemed AMA?

MR. SHUSTER: Well, that's the effect that the misrepresentation has on the value of the loan in the

market. So that is what -- in the market and -- that is what Lehman, for example, says in its declarations on the subject. It says that when you have a misrepresentation of income, it has a material and adverse effect on the value of the loan. The loan cannot be sold into a securitization except at a substantial discount. Those are the words Lehman uses.

THE COURT: But that --

MR. SHUSTER: That language --

THE COURT: But that goes back to what -- I think what Mr. Cosenza was saying about for the purposes of selling it into a securitization versus calculating damages in a put-back context. I think the point made was that those are different.

MR. SHUSTER: Okay. Well -- and I'll -- I'll be happy to take that on --

THE COURT: I'm going to try and stop interrupting.

MR. SHUSTER: No, no, not at all. I mean, I'm happy to engage on these issues and, to us, it does --

THE COURT: It doesn't matter.

MR. SHUSTER: A loan is a loan.

THE COURT: Okay.

MR. SHUSTER: And when Lehman says, sure, it's a whole loan, it's a standalone, but they're the ones who are

saying I can't put it into a securitization except that it's at a substantial discount. But it was put into these securitizations without that discount. And so there was an effect -- the trusts overpaid for those loans. They paid a higher price than they should have paid. That's a continuing effect. Whenever it's assessed, it's always true that they paid a higher price than they should have paid.

So we agree that the purpose of the hearing is to estimate the value -- I have a roadmap here. First item in the roadmap is the purpose of the hearing and that the purpose of the hearing is to estimate the value of the trustee's RMBS claims. We're happy to take on the standard of what would have happened to these claims because had they gone all the way through the protocol, because we believe we do have, as I said, breach -- evidence of breach on a loan by loan and breach by breach basis.

So we prefer a methodology that actually evaluates the evidence that we've developed and are submitting rather than one that is based on applying haircuts and discount percentages. We'd rather see something that is more closely tethered to the proof.

So the trustee's claims have four elements. First is the representations and warranties, then evidence of breach of those representations and warranties, meeting the material and adverse effect standard and the purchase price.

And the repurchase protocol makes clear that where there is a breach of the representation of warranty that has a material and adverse effect, the remedy is either cure, which is not at issue here. And really, these types of breaches can't be cured. There are certain types that can be cured but this type can't be cured. Cure -- within the first two years, the sponsor can substitute in a different loan under the REMIC regs and then, alternatively, repurchased.

So the no untrue statement representation we looked at a moment ago. The only comment I'll make is that it is a broad and sweeping representation of the truthfulness of the documents that were submitted for loan underwriting. The statement is that there is no untrue statement. There is no material.

Then the other principal representation and warranty that we rely upon, particularly for the borrower, breach is predicated on borrower misstatements or omissions is the no-default representation. This is also a standard representation in these deals and it says there's no default under the mortgage or the mortgage note. And then, in the mortgage and the deed of trust, there are borrower covenants. One of the borrower covenants expressly provides the borrower shall be in default if he gives materially, false, misleading or inaccurate information or fails to

provide accurate information and that material misrepresentations include, but are not limited to, representations concerning the borrower's occupancy.

So those are the principal representations that we rely upon. Those -- or representations were not made by chance. They're in every single one of these securitizations. They were a necessity for marketing securities to investors. Judge Cote commented in the FHFA, the Deutsche Bank case, that are used -- these representations are used to market and sell securities to investors. And they're made, in part, because investors, given the nature of these securitizations, the speed and the confidentiality, the information to investors were not in a position to, and it was not the practice, for the investors to do due diligence on the loan by loan basis.

The securitization documents allocate the risk of loss on breaching loans to Lehman.

I'm going to put this down 'cause whoever is making this app is doing it better than I am. It's good to have colleagues.

THE COURT: Younger colleagues.

MR. SHUSTER: Yes, indeed.

So -- which most of mine are.

So the securitization documents allocate the risk of loss on breaching loans to Lehman. If there's a loan

that breaches this representation or warranty, that's Lehman's problem. If the loan doesn't breach the misrepresentation and warranty but doesn't perform, that's investor's problem. That's essentially the allocation of risk that is reflected in --

THE COURT: But --

MR. SHUSTER: -- the reps and warranties.

THE COURT: -- there's also the AMA.

MR. SHUSTER: Yes. But the --

THE COURT: You're not intending to leave that out.

MR. SHUSTER: No. I'm not intending to leave that out. The breach of representation on warranty has to have a material and adverse impact, for sure. But that does not mean that the trustees have to show that the breach caused the loss, that it -- and, in Judge Castel's words, that there was a loss. In fact, it was caused by the breach or that the breach caused the loan to default. That's not part of the equation. There's an -- it has to have some impact on the value of the loan but it does not have to cause the loan to incur a loss or to default.

So --

THE COURT: Just thinking about it. Just thinking about what it would mean at origination, say, in 2003, right, for there to be, I don't know, a six percent

misrepresentation on income. Right? And now here we are in 2017, or wherever you want to start the countdown clock, 2015, whenever the -- for the purposes of my hypothetical, you understand the point.

MR. SHUSTER: Yes. Yes.

THE COURT: And then you go and look at the -- you go and look at what you have and you have a loan mortgage history, perfect payments every month --

MR. SHUSTER: Right.

THE COURT: -- to this day.

MR. SHUSTER: Right.

THE COURT: Right? So your position is doesn't matter. Breach, greater risk, put-back, doesn't matter in terms of the riskiness of the loan that you have this -- I'm making this up.

MR. SHUSTER: Yes.

THE COURT: Just for illustrative purposes.

MR. SHUSTER: Yes, yes. Of course.

THE COURT: That you have this countervailing body of information that says, wow, this is a really good borrower. Right? I mean --

MR. SHUSTER: I --

THE COURT: You agree with that, right?

MR. SHUSTER: I agree with that.

THE COURT: Okay.

MR. SHUSTER: If it had a material and adverse effect on the risk of loss or on the price, the value of the loan, all of which sort of amount to the same thing, risk value, are two sides of the same coin, then, yes, that's true. I will say that that scenario is very much the exception rather than the rule.

So, you know, all -- but for --

THE COURT: I was stating it in --

MR. SHUSTER: But it pushed --

THE COURT: -- the extreme --

MR. SHUSTER: -- yes.

THE COURT: -- for -- yes.

MR. SHUSTER: Yes. I absolutely --

THE COURT: Yes.

MR. SHUSTER: I would say that.

THE COURT: Okay.

MR. SHUSTER: So evidence of breach.

We have two broad categories of breaches as we said in our pretrial brief. We called -- or the breach is predicated on borrower misstatements and omissions, the big four. And those are income, debt, occupancy, misrepresentations and excessive DTI. And then there are breaches that tend to be based on lender omissions of documents or provision of defective documents.

So these and the categories of breaches -- and

there are other breaches. There are other miscellaneous categories. These are the large -- largest ones that comprise the vast bulk of the claims.

So there are different processes for establishing these breaches. For the borrower breaches are predicated on affirmative evidence of breach. The loan reviewers were instructed to, and did, attempt to verify whether the information set forth, the borrower information set forth in the loan application was accurate. They did that by looking through the loan file. And then, to the extent necessary, going and consulting various third party sources that, in our view, are in customary and wide use in the industry. Lender breach -- and the borrower breaches are always predicated on the two representations and warranties that we looked at a moment ago.

Lender breaches -- there are more potential reps and warranties that come into play compliance with federal law, compliance with state law, truth in lending. There might be a specific appraisal breach, appraisal rep. There might be another rep that applies. And it's a matter of mappings or reps to that specific transaction. Determining what documents are called for, attempting to identify whether those documents are in the loan file. Sometimes in these loan files a document will appear in partial form multiple times. They have to be signed. Is it signed? Is

it there? But that's the process. It's trying to prove a negative in some way and to determine whether the documents that are required to be there are there rather than on the borrower's side, you have some data points, you attempt to verify them based on what's in the file or what you can determine from third parties.

THE COURT: How do you -- on a wholesale basis and the missing or defective documents --

MR. SHUSTER: Yes.

THE COURT: -- category -- let's try to make it easier. Missing.

MR. SHUSTER: Yes.

THE COURT: How do you get over the issue of that was then, this is now?

MR. SHUSTER: So --

THE COURT: I mean, that's a tough issue --

MR. SHUSTER: It is.

THE COURT: -- right?

MR. SHUSTER: It is. And it's one that Judge Castel struggled with and it is. So the -- ultimately, the way we get there is by trying to establish that the loan file is substantially complete but it's missing -- you know, it partly is a function of what else is in the loan file. So that's one way that we deal with it.

I will note that on 50,000 of the loans at issue

here, they're Aurora loans. And Aurora acknowledged -- Lehman acknowledged in the Protocol that the Aurora loans were -- loan files were substantially complete. But there are other loan files, too. We'll put on an expert witness, Bernette (ph) who will testify to how servicers maintain loan files. They're not cavalier with loan files. They try not to spill coffee on loan files. And in the chain of custody that Mr. Cosenza showed you, there's the mortgage broker and the borrower sitting at a table. It goes to the originator. It goes to the funder which is Lehman Bank in the vast number of cases. It goes to the sponsor, then from the sponsor to the servicer. So actually, in principle, nothing should get lost along the way even though we know in fairness and candor that that happens. But the way we deal with that is based on other indicia that the loan file is otherwise complete.

THE COURT: So you -- there are other indicia that the loan files are otherwise complete and therefore you're asking me to draw an inference --

MR. SHUSTER: Correct. Yes.

THE COURT: -- that in otherwise good files, if this is missing, I can conclude that it was actually missing.

MR. SHUSTER: Yes.

THE COURT: Okay.

MR. SHUSTER: That's fair.

THE COURT: So that's that. And then on the AMA prong, you are -- let me ask it as a question. So take a failure to provide -- that there's not an indication that there was a right of rescission provided. Are you going to be putting in evidence that that, absence of a document, assuming that it was an at origination thing -- right? We've gotten over the first hurdle. Now we're at the second hurdle, right? So now are you going to be putting in evidence or giving me a basis on which to find that that fact, the absence of the right of rescission, had an -- has a continuing adverse material effect on the loan?

MR. SHUSTER: Yes. So we would say that, first, approximately 75 percent of the missing document breaches, the breach is deemed material. So by the document -- by the governing documents.

THE COURT: Okay.

MR. SHUSTER: So we have in 25 percent. And then, yes. Our experts will opine that if that document is missing, it has a material and adverse effect on the value of the loan --

THE COURT: But that's a truism. So what is the -- why? What --

MR. SHUSTER: Because it affects the ability to --

it introduces risk into the value of the loan because it affects the ability, for example, to enforce the loan terms, to foreclose on the loan, to enforce the terms against the borrower and so forth. If --

THE COURT: Meaning that you go to foreclose and there's no right of rescission in there. And the --

MR. SHUSTER: If there's not --

THE COURT: And the borrower says

MR. SHUSTER: That was --

THE COURT: -- you're out of luck. Free house.

MR. SHUSTER: Yes.

THE COURT: There's no right of rescission in the file.

MR. SHUSTER: Well, not free house but they can --

THE COURT: You can't enforce.

MR. SHUSTER: You can't enforce or they can make it difficult or you have to incur more expense or you have to enforce on different terms. That's where the material -- and the value of the loan in the market -- if you -- you know, there are scratch and dent securitizations where loans that are --

THE COURT: That's a new one. What does that mean?

MR. SHUSTER: Loans that are more necked up where they are known to be breaches of representations and

warranties or defective documentation. That's where those go. You know, it's the Island of Lost Toys. But that's where those go. And they --

THE COURT: But what --

MR. SHUSTER: And they fetch a lower price.

THE COURT: Okay. So -- but --

MR. SHUSTER: That's what our -- that what our --

THE COURT: Now --

MR. SHUSTER: -- experts will say.

THE COURT: And not keeping my promise to interrupt you less.

MR. SHUSTER: I welcome it.

THE COURT: I'm just trying to stick with you here. But now it does sound like not only on the borrower/breach category which, intellectually -- even though I obviously haven't made a decision yet -- on the deemed AMA and the proof of AMA, it sounds a lot worse, kind of we're at large where you have a 50 percent misrepresentation of income. That sounds bad, right? Doesn't sound as bad to that piece of paper missing in the file. But it sounds like you're leading me to demonstrate breach. You have adverse material effect. It does not sound like those are two separate things that you're going to say -- that you're going to, in fact, show or feel that you need to show in every category.

MR. SHUSTER: Well, I'll say two things. One, if where you end up -- where Your Honor ends up is that 50 percent income misrep sounds worse than a missing document, I think that's a fair statement. But at the same time, we do show this on a loan by loan basis. It looks like we're just saying it 'cause we're saying it for so many loans. But, in fact, this is the industry custom and practice. This is the legal standard. It's the one that our experts will say is --

THE COURT: I'm sorry. We're competing with the garbage truck now.

MR. SHUSTER: So --

THE COURT: I'm trying to understand. Whether -- something being the industry standard doesn't answer the question as a matter of law. What do I do with a document in MLSAA, or whatever the acronym is, that says you have a material breach that adversely affects, present tense, the value of the interest holders, the certificate holders, whatever --

MR. SHUSTER: Yes. Well --

THE COURT: -- it says.

MR. SHUSTER: We have to rely for that on expert testimony that if a Truth in Lending Act disclosure is not there or defective and that it's not deemed material, it's material on this loan because it has -- because it increases

the risk on the loan and it diminishes the value of the loan. So it is a distinct showing and a distinct finding but -- so that's the way I would --

THE COURT: Okay.

MR. SHUSTER: -- I would say it.

So on -- if we could move on to the -- what we call the big four breaches. They are overwhelmingly income and debt. That's by far the largest the number. We have -- this is really self-explanatory but nine billion, roughly 9 point almost 2 billion of the 11.6 billion of the income, debt, occupancy and DTI breaches. And most of it is income and debt.

So the trustee's loan review process. We have receipts of claims files from the servicers and then production and review of claim files by the trustee. We can fill the rest of that in because I'm only -- I'm stopping at 1 for this purpose.

So the trustees were required to obtain and review loan files and that's what they did. And then if we look at the next chart, so the trustees reviewed originally 171,000 loan files. I think it's important -- we think it's important for purposes of assessing the trustee's loan review process and the good faith and punctiliousness with which they approached the Protocol, that they went through the loan files and for 77,000 loans, which is almost half,

they found no breach. So half of 171,000 is 85,500. And on 77,000 loan files, the trustees found no breach. No missing documents, no inconsistency in income, debt, occupancy or DTI. And they did not put those loans through the protocol. They found breaches on 94,506 -- or what we have here rounded to 94,000 loans. And now the number that's presented for estimation is 72,500. About 8,000 of the loans that dropped off dropped off because there's an opt-out trust that has the claims on 3,000 loans. Then there are terminated trusts and there are paid off loans. And then there is the withdrawn loans that has received not inconsiderable attention. So that's how we get to the number that's -- the number of loans that's presented for estimation. I will come to the withdrawn loans in a bit.

The loan reviews were conducted by experienced firms supervised by Duff & Phelps. So Duff & Phelps interviewed, was engaged by the trustees to manage and supervise the loan review process. I think it interviewed eight firms to determine whether they had the expertise and capacity to participate in the loan review. And these are the ones that they selected. These are well known in the industry. And at least a few of them, their work has at least been cited, been reported decisions. I mean, they are established loan review firms in the industry.

The loan review process then, as reflected here in

this engaging funnel chart, 171,000 loan files. The loan review firms performed a complete review of the loan file and an initial loan review on a second level -- loan review to verify borrower information and to ascertain whether there were missing or defective documents called for by the representations and warranties for any particular deal.

We will have two witnesses testify to the trustees' loan review process which they're both originally from Duff & Phelps. Mr. Esses will testify as a fact witness; Mr. Aronoff as an expert witness. Duff & Phelps performed two levels of QC as I've described earlier on the loans. 94,000 originally made it through. 77,000 were found not to be breaching.

Just an observation. Mr. Cosenza mentioned that he finds it highly unusual in his experience that someone who participated in the design and execution of the loan review should now be opining on the validity of the claims. But I can honestly say that in these cases, that's how it's done.

Let me start with the reported cases.

So in the MARM (ph) case, the testifying witness was Ira Holt. He designed and executed the review and then testified to it.

THE COURT: But hold on. But hold on --

MR. SHUSTER: Yes.

THE COURT: -- 'cause this is an important point. In those cases, I find it not surprising that he would testify to it as to here's what we did. But this is different because in this case, we have the issue of using the process itself to extrapolate the number. So in that sense, it is more like I did a great job over there. When I was first hired to design this protocol, it was a great design.

MR. SHUSTER: I don't --

THE COURT: It's different. No?

MR. SHUSTER: I don't see it.

THE COURT: Well, maybe --

MR. SHUSTER: And, you know --

THE COURT: -- you could make a note --

MR. SHUSTER: Yes.

THE COURT: -- for some time later on --

MR. SHUSTER: Yes.

THE COURT: -- to show me --

MR. SHUSTER: Yes.

THE COURT: -- in some of the cases --

MR. SHUSTER: Yes.

THE COURT: -- which I have read -- see, as indicated by the yellow page --

MR. SHUSTER: Yes.

THE COURT: - marked. You could show me in the

cases where that's a thing that was done that is less remarkable than Mr. Cosenza would have me believe.

MR. SHUSTER: Yes.

THE COURT: And then the other thing is, and maybe you were going to get to this, Mr. Cosenza made a big point of highlighting the fact that for at least one of the two levels of QC, there was no mucking around in the loan files. Which is also interesting because I don't really understand how you could QC something without at least, on some level, kind of spot checking the underlying data. So if you could address that, too --

MR. SHUSTER: Yes.

THE COURT: -- I would be grateful.

MR. SHUSTER: Yes. So just to finish the thought on --

THE COURT: Yes.

MR. SHUSTER: -- Mr. Aronoff, this is a bigger loan review process. But it was always anticipated that, at the end of the day, the trustees might have to prove their claims in an adversarial process. And the expert would have to opine on the appropriateness of the process, the extent to which it conforms to industry practice and so forth.

In that respect, it's bigger but it's no different in design or in principle from what was done in those other cases. I'm highly familiar with pretty much all the cases.

And it's done -- I mean, I'm liaison counsel in part 16, the commercial division and there's about --

THE COURT: That's lovely

MR. SHUSTER: Well --

THE COURT: You're not an expert --

MR. SHUSTER: No. But -- but --

THE COURT: -- and I only -- I only know what I'm going to -- what you're going to tell me.

MR. SHUSTER: The only reason I say that is because my friend on the other side said this is unique in his experience. And I'm saying it's not in my --

THE COURT: Okay. But I can't take your word for it.

MR. SHUSTER: Of course not.

THE COURT: You have to --

MR. SHUSTER: Of course not. Mr. --

THE COURT: And I'm saying that --

MR. SHUSTER: Yes.

THE COURT: -- please make me smarter --

MR. SHUSTER: Yes.

THE COURT: -- on the points.

MR. SHUSTER: Yes. Yes.

So as far as the QC goes, the first level of QC was that the QC team looked at the claim package, looked at whether it was complete, whether the information -- the loan

application was in there and whatever other information bore on the issue of whether there was a borrower misrepresentation. So that had to be reflected in the claim package. And that would have been gleaned from the loan file or it would have been obtained from third party sources. And then whether the description was correct, whether the mapping to representations and warranties was correct and whether the breach claim appeared to be -- the alternative to that is essentially to entirely re-underwrite the loan file. And that would -- in our view, there were two levels of review at the loan firms themselves. It's not a defect in the design of their review not to do that, not to have the first level of QC go back through and re-underwrite the loan file entirely.

THE COURT: So let me ask a different question and maybe whosever operating the clicker could click back to -- I'm not going to be able to find it. There's a slide that shows Duff & Phelps and all the firms that --

MR. SHUSTER: Yes. That's --

THE COURT: -- actually did the underwriting.

MR. SHUSTER: Right. Couple slides -- right.

THE COURT: So -- yeah. That's the one.

So another point that Mr. Cosenza emphasized was no uniform standards. So you can agree or disagree with that. That's point number one.

And then point number 2 is, so how do you QC -- are you looking for -- are you QC'ing Digital Risk for what Digital Risk did across their portfolio versus comparing what Digital Risk did with what Opus did and trying to generate some kind of a consistent answer?

MR. SHUSTER: So I won't say that the reviews were absolutely uniform in all particulars but instructions were given to the loan review firms and how to carry out the reviews.

THE COURT: And there'll be evidence on that?

MR. SHUSTER: And there will be testimony on that. Fact testimony and expert testimony. And there was also regular weekly or almost weekly calls and reviews between Duff and the review firms where to the extent that revisions or modifications had to be made or questions came up that they were addressed. So there was considerable -- you know, I won't say 100 percent but considerable uniformity among the review firms in terms of what they were told to do and what they did.

Most fundamentally, they were told to do two things. Look at the loan application, verify the key information that's in there by looking through the loan file or by going to any one of a number of third party sources. And, separately, identify the reps and warranties for that deal, determine what loan file -- what documents were called

for and determine if those documents are in there in their proper form, whether they're there, whether they're defective. Broadly speaking, those were the instructions that were given.

THE COURT: Okay.

MR. SHUSTER: So the loan review process -- I think I've been over this now. And if I haven't been over it earlier, I just said it again. So let's, if we could, look then at income.

So misrepresentation of income. So these are the types of proof that the trustees relied upon. I'm going to shortly show what these translate into from a dollar number standpoint. They are ranked here in order from most used to least used. And, you know, we will have certainly expert testimony that these are commonly and widely used in the mortgage industry. Actually, at various phases. Loan origination and underwriting servicing of loans, forensic reviews, put-back claims. These types of proof have been accepted by other courts including, in particular, the three federal courts that have tried cases in this area: Judge Cote in FHFA v. Nomura, Judge Castel and Judge Rakoff. And from our point of view, importantly --

THE COURT: So Rakoff was a monoline, right?

MR. SHUSTER: Rakoff was a monoline -- yes.

THE COURT: I know you don't think it makes any

difference --

MR. SHUSTER: I don't.

THE COURT: -- but --

MR. SHUSTER: I don't because they're the same reps and warranties and the same remedies. I mean, that -- you know, that's --

THE COURT: Well -- I hear you.

MR. SHUSTER: That's my expression but okay.

So -- and then importantly to us, we think, in corroborating what we say, these types of evidence were used by Lehman and Aurora in prosecuting their own put-back claims. And in many instances, they weren't merely used but Aurora's policies and procedures manuals say use these sources of evidence.

So we've looked generally -- we've already looked at this for purposes of the exemplar so I don't need to dwell on it here other than my point is only that generally, Lehman addressed types of evidence in a generic or categorical way rather than in a granular and specific way where it said, no, the loan -- the tax return doesn't say that or, in fact, this borrower earned a different amount or so forth. And I think, from our point of view, that's helpful in that it delineates -- it sort of delineates disputes, fundamental disputes, about the sufficiency of different types of evidence.

So then we get to -- this is where we sort of map the evidence for income to dollar numbers. So it's a bit of a slog but if you look at, say, Your Honor, salaried employees -- and we rely on same year accrued for salaried employees, you can see the number of loans that are supported by tax return evidence. And again, that's same calendar year evidence.

Bureau of Labor Statistics evidence, bankruptcy filings, audit documentation typically as a credit report or a similar document, W-2s and --

THE COURT: Well all know how good the credit rating agencies operate, right?

MR. SHUSTER: Well, they may not be good maintaining information but we think they're good enough providing information. So whether they protect its privacy is another matter. But they -- certainly, credit reports are widely used and relied upon in the mortgage industry.

Your Honor can see that most of the dollars are in the top sort of half a dozen. And the same is true for salaried employees. Sorry. Just pop back up -- near year. You've got tax returns, bankruptcy documents. It's almost all I those top three or four categories.

THE COURT: How do you define near year?

MR. SHUSTER: Near year is --

THE COURT: Two years or less.

MR. SHUSTER: It's two years or less. Exactly.

Okay. Then self-employed. We have again, tax returns, bankruptcy documents are by far the biggest items for same year proof and for near year proof.

So that's --

THE COURT: So for the bankruptcy documents --

MR. SHUSTER: Yes.

THE COURT: -- what you're saying in broad outline is that they represented on their loan application that they made $100,000 a year. And then either same year or near year, they file for bankruptcy. And on their -- on some bankruptcy document, they state lower income?

MR. SHUSTER: Yes. So it's not same year and near year for bankruptcy documents. It's actually not when they filed but what they say about -- are they making a statement about the calendar year or we say a subsequent. Their income in the calendar year in which the loan was made or a subsequent year. Just for clarity, that's what same year --

THE COURT: Right. But I'm just trying to --

MR. SHUSTER: Yes. But -- yes.

THE COURT: I'm just trying to understand --

MR. SHUSTER: If they have in their financial statement, if they represent my income in 2007 was x and that is, you know, materially lower than what was represented on the loan application then we would rely on

that document to establish an income breach unless there's something else in the file that shows --

THE COURT: But how would you be able to tell if someone has a job and they apply for a loan in January and the loan closed in March and then in June, they were -- you know, there was a reduction in force or they got laid off and then they put that fact on their bankruptcy document, what -- I mean, that's not --

MR. SHUSTER: No. That --

THE COURT: That's not a breach.

MR. SHUSTER: That may not be sufficiently -- if they say that much then you may not -- we may not have put that forward as a breach.

THE COURT: But you wouldn't -- you wouldn't see that in a -- again, we're getting really into the weeds here --

MR. SHUSTER: Yes.

THE COURT: -- whether it's a Chapter 13 or a Chapter 7 or an individual 11, whatever it is. You wouldn't necessarily see that sweeping a description of things in a -- what you're calling a bankruptcy document.

MR. SHUSTER: Well, typically -- well, first, they're --

THE COURT: Remember who you're telling "typically" --

MR. SHUSTER: Yes. No. Of course.

THE COURT: -- okay?

MR. SHUSTER: Yeah. No. Of course. I hope you find bankruptcy filings sufficient and probative. But --

THE COURT: I'm just trying to understand --

MR. SHUSTER: -- oftentimes --

THE COURT: -- how --

MR. SHUSTER: -- there's other information in the bankruptcy filing that may indicate whether the borrower has the same job, for example.

THE COURT: Sure.

MR. SHUSTER: But the income is actually lower than the borrower represented it to be. Sometimes there's other corroborating evidence in the file. Typically, a bankruptcy document is in the file either because it's been provided to -- if it's in the loan file -- and that's not always the case -- sometimes you go and get it off the docket. But oftentimes, it's in the loan file and it's either been obtained by the servicer for purposes of verifying the borrower's income or debts to determine whether to make a loan modification and, if so, in what way. Or it's provided affirmatively by the borrower for the same purpose. So oftentimes, it's rarely that -- you know, it is sort of one naked piece of information that when you look at it, you say I'm not comfortable that this alone establishes

the borrower's income.

THE COURT: Okay. Why don't we move on?

MR. SHUSTER: And, you know, we'll look at examples and they'll bring forward examples. But generally, the information where we put it forward from a bankruptcy filing, we think it shows that the borrower was in the same job or had the same job for enough of the calendar year that you can draw reasonable inference that the borrower's income from that job was not what the borrower represented it to be on the loan application.

So that is -- so then Your Honor asked a question about whether we would show the magnitude of income breaches. And so here is a breakdown. As the Court can see, there's a -- the smallest number actually is in the 5 to 20 percent range. And then it gets bigger quickly from there. We could, you know, break it down above 121 percent but we make the point, you know, it goes up from there. But generally, we're talking about significant overstatements of income by borrowers. And to borrow a word from Judge Castel, a misrepresentation of income of a certain magnitude bespeaks of intent and these are substantial overstatements of income. Not that it's our burden to establish intent. It is not. But we're talking -- you know, we -- we're talking about meaning overstatements of income.

So the integrity of the process. And I may be

belaboring this at this point, but we have the loan review firm that verified the income. And I'm just focusing on income as one category and one aspect of the process. We had the QC I and II at Duff & Phelps.

Now the -- we did bring someone in. We did bring in an expert witness to run an independent check on what had been done. That's Chip Morrow. You saw snippets of Mr. Morrow's testimony during Mr. Cosenza's opening. Mr. Morrow has 40 years of experience in loan origination and underwriting. He reviewed a sample of loans as a --

THE COURT: How did he get the sample?

MR. SHUSTER: The sample was selected for him using techniques designed to ensure a random and representative sample by Dr. Schwert. I forget his first name but he's an econometrician on the faculty -- the finance faculty at the University of Rochester. He will testify to how the sample was polled. We're not using the sample and the breach rate, the agree rate of Mr. Morrow. We're not arguing that that's a breach rate that the Court should rely upon. It's an agree rate. It's an independent check on the integrity and reliability of the trustees' review, the trustees' process, the trustees' evidence. It's for that purpose that we're putting forward Mr. Morrow.

THE COURT: But this was not done -- I mean, maybe this is no different from any other expert. But this was

not double blind in any sense, right? He knew. He knew that best case scenario was close to 100 percent, right?

MR. SHUSTER: I don't know what that means. You mean that he was --

THE COURT: What that means?

MR. SHUSTER: No. I don't think he -- I mean, you'll have to evaluate him and his independence --

THE COURT: But it wasn't -- it wasn't a double blind evaluation. Here are a set of loans. Right? Determine whether or not there was a breach. I mean, he --

MR. SHUSTER: He was running a check --

THE COURT: He knew the destination --

MR. SHUSTER: Well, I don't know if he --

THE COURT: -- when he set out on the journey.

MR. SHUSTER: I don't know if he knew the destination. He knew what the population was that he was looking at. He knew that the sample was drawn from a population of loans that had been identified as breaching. So that's fair. But I think he -- you know, it's our view and you'll have to evaluate -- the Court will have to evaluate his credibility and integrity but he made his own call. Once he looked at the loan file and once he looked at the claim, he decided whether or not he agreed that there was a breach. He's a pretty independent guy and that's what he did.

So --

THE COURT: There was no, you know, control group where he was given loans that were -- a loan population where there were no breaches and breaches.

MR. SHUSTER: I don't believe so. He was just given -- he was -- the breaches that he got were selected from our top 12 breach categories using --

THE COURT: Okay.

MR. SHUSTER: -- a random number generator, essentially, and that was the sub-population that he reviewed for this purpose.

THE COURT: Okay.

MR. SHUSTER: So misrepresentation of debt.

THE COURT: Do you want to take a break, Mr. Shuster?

MR. SHUSTER: No. I'm fine. I'm just --

THE COURT: Well, you let --

MR. SHUSTER: -- mindful of the time.

THE COURT: No, no, no. You --

MR. SHUSTER: If I'm going on too long --

THE COURT: But you let me know when --

MR. SHUSTER: So far so good.

THE COURT: -- you want to take a break. Okay?

MR. SHUSTER: Thank you very much.

So misrepresentation of debt. Same type of thing.

Same category -- similar categories of types of proof, again, organized in order of most commonly used. We'll have expert testimony that they're used in the industry. We'll show that they're accepted by the Courts and that they were used by Lehman in the ordinary course in pursuing its put-back claims.

So here, I'm going to walk through a debt exemplar in a moment just for illustrative purposes. Here is a excerpt from the claims tracking spreadsheet. And this shows that a review of a merge report revealed undisclosed mortgages.

And then we have a response from the plan administrator that it relies on an inadmissible uncorroborated report. So it's sort of rejected MERS as a type of evidence.

Now I'd like to actually jump ahead to the exemplar and then I'll come back to the breakdown. So if we look at the exemplar, it relates to a property in Spring Park, Minnesota. The borrower, Joseph L., $84,000 loan on a primary residence taken out in August of 2006. The loan application calls for the borrower to disclose his or her debts. These are the debts that the borrower disclosed for different debts totaling -- a total unpaid principal balance of $21,303. And then there's the borrower's name and signature.

We then have excerpts from the evidence of breach that was provided in the claims package.

So "Data Verify" is a service that runs checks using the borrower's social security number and gives you various reports including MERS. So it's a MERS report that was obtained through a data verify search. The MERS report shows the same borrower and it shows "Undisclosed Mortgage Debt of the Borrower".

And then there's a credit report also run with the borrower's social security number. And the credit report also shows two items of undisclosed pre-closing debt also taken out in August of 2006. And again, the loan closed -- the subject closed on --

THE COURT: You know, I'm just trying to --

MR. SHUSTER: Yes. Yes.

THE COURT: I'm just --

MR. SHUSTER: Sorry. Yeah. Let me slow --

THE COURT: I'm just trying to follow this.

MR. SHUSTER: Yeah. So the subject loan, if we go back to the cover page, closed on August 24, 2006.

THE COURT: Okay.

MR. SHUSTER: And then if we jump ahead to the MERS report on the left. And you look in the upper left corner of the MERS report, there's a Rich --

THE COURT: A-14.

MR. SHUSTER: -- A-14.

THE COURT: Right.

MR. SHUSTER: Right. And the same is true for the second item. And the credit report shows, on the top line, the fourth column over, "Opened". It shows that it opened in August of 2006, the loan.

THE COURT: Okay. Tell me once again when did this close?

MR. SHUSTER: The loan closed on August 24th, 2006.

So --

THE COURT: Okay.

MR. SHUSTER: -- this is the sort of evidence that we relied upon. Now if we could just back up to the same year/near year breakdown, I have the same breakdown -- we have the same breakdown for misrepresentation of debt that we did for income. And a good deal of the pre-closing mortgage debt is based on these MERS and data verify reports or on credit reports. And then there is pre-closing installment debt which is to say non-mortgage debt. And then there is post-closing mortgage and installment debt and that is established yet similar types of evidence.

So then if we jump past the exemplar to the magnitude chart, this chart breaks down the magnitude of the nondisclosed debt breaches that we're looking at. And as

the Court can see, most of them are in the $20,000 or more category.

The debt went through -- the misrepresentation of debt breaches were subject to the same loan review and QC process and were also reviewed by Mr. Morrow.

Occupancy. Same categories of evidence. We make the same points in terms of their industry use, judicial acceptance and use by Lehman. Here, we have -- again, we pulled out an example that's based on a tax return but there are, you know, occupancy breaches that are supported in other documents. But here, it says that the loan file contained post-closing 2006 and '7 tax returns along with the Schedule E which reflected the subject property as a rental when it was supposed to be the primary residence.

The response was that the tax return evidence is unreliable and insufficient. And again, what the plan administrator did not say is no, it's not in there or it doesn't say what you say it says.

So the -- here is the loan. Borrower, Antonia E. Property in -- sorry. I skipped over the map -- in Northwest 24th Avenue in Miami, Florida. And there are the details concerning the loan which had a closing date of June 12th, 2006.

So we have the loan application which shows that the property will be the borrower's primary residence, the

subject property address and the borrower's present address. So the borrower's present address is Southwest 14th Street. We're relying on, as I mentioned, obviously, the no untrue statement and no default reps. But there is also what we have here is an occupancy covenant that's in the mortgage where the borrower is required to occupy within 60 days and then for a full year and for the vast majority of the occupancy breaches, we have occupancy affidavits where the borrower affirms that, under oath, that he or she will occupy the property and acknowledges that not doing so is a breach of his or her covenants.

So the evidence then of breach, the tax return, it's a 2006 tax return, a 1040. Again, the loan had a closing date of June of that same calendar year. And the borrower's address is listed at her prior address which is on Southwest 14th Street. So that establishes that she did not occupy the property within 60 days and certainly not continuously for a year. And then there is, moreover, in the same tax filing a Schedule E that shows that the subject property was used as a rental property and generated rental income.

And then there is evidence from 2007. Again, a tax return to the same effect showing the borrower's prior address and showing the subject address -- prior address as her residence and the subject address as her rental home.

So the story the loan file tells is the one that we just saw. It went through the same loan review and QC process and was -- it's not that this loan was passed upon by Mr. Morrow, in particular, but he looked at property occupancy breaches in the course of his review and had the agree rate that's specified there.

So then moving to breaches that are predicated on more on lender conduct which is to say missing or defective documentation. This is set of those breaches breakdown from a numerical standpoint. They're principally in these four categories, HUD-1, till right of rescission and appraisal. And they break down between Aurora-originated loans and other loans and those -- I gave you that -- Your Honor, that number earlier. And the percentage that are deemed material and adverse.

So, you know, now might be a good time --

THE COURT: Okay.

MR. SHUSTER: -- for a break, I think.

THE COURT: You have a rough estimate of how --

MR. SHUSTER: -- for the sake of all concerned.

THE COURT: -- much longer you have? What page are you on?

MR. SHUSTER: Let's see. I'm on page 70-ish of 120. I don't know. Maybe 45 minutes.

THE COURT: Sounds good. Okay. Let's take a 10-

minute break and then we'll resume.

MR. SHUSTER: Thank you, Your Honor.

(Recess from 3:17 p.m. until 3:41 p.m.)

THE COURT: I apologize. What happens when I go back in there is 50 things -- please have a seat -- 50 things that people want me to do instantly, so I apologize.

MR. SHUSTER: Not at all, Your Honor. Thank you. May I continue?

So turning now to Lehman's process, Lehman declined to review a third of the loans, what it refers to as the on-hold loans which I will come to in detail. So a third of the loans did not get reviewed in the protocol at all by Lehman, 32,000 loans.

THE COURT: How does that map to what -- the loans that are being presented for estimation?

MR. SHUSTER: 24,000 now. So it's 24 --

THE COURT: Say it again.

MR. SHUSTER: 24,000 of the loans being presented for estimation were not reviewed by the --

THE COURT: So that's a third.

MR. SHUSTER: Yes.

THE COURT: 24 of 72.

MR. SHUSTER: Yes.

THE COURT: Okay.

MR. SHUSTER: Yes.

Lehman's loan review firm was Recovco. Recovco reviewed loans and if it determined that there was no basis for a breach, it set the loan aside. If it determined that there might be a basis for a breach, it elevated the loan up to Rollin Braswell, Lehman's trial counsel's firm, to review and make a final determination on the loan. That is described in detail in Mr. Grice's expert report and in the testimony of Mr. Trumpp and Mr. Grice. And Lehman ultimately ended up with something below a 2 percent acceptance rate. And that remains the acceptance rate today. If you just take 72,500 loans and the fewer than 2,000 loans on which Lehman has accepted breaches, the acceptance rate remains where it is. We don't think that acceptance rate is credible for a variety of reasons some of which I will come to.

Lehman -- so, you know, one of our principal points in asking the Court and suggesting that the Court can resolve common disputes -- general disputes that are common to groups of loans is that we put forward various types of proof and we get a sort of a generic response for that category. What we didn't get are evidence to actually refute the breach findings that the trustees put forward.

So it's -- was Aurora's practice -- in fact, it was in Aurora's policies and procedures manuals relating to put-back claims. And then it was in the letters that it

sent out making put-back demands that it asked that the obligor either provide evidence to refute our findings and if you cannot provide evidence to refute our findings then you must repurchase the loan. But what we got, for the most part, back, what the plan administrator provided were the sorts of responses that are quoted on the next chart as to categories or types of evidence.

So -- but these same types of evidence, tax returns, credit reports, bankruptcy documents, verifications of employment, work number, Acurints and so forth, were relied upon and put forward by Aurora in support -- or Lehman -- LBHI -- in support of their own put-back claims.

So here is an affidavit submitted by an LBHI employee referring to tax returns that prove a borrower breach. And obviously, we will go through these in greater detail and our cross-examinations of Lehman's witnesses -- which is not revealing estate secret. We all know that we're going to be talking about these documents.

Here is a letter from an Aurora employee, Sean Kelmurray (ph), the borrower's bankruptcy filing reflects how much the borrower made. And that's put forward as the basis for the assertion of a violation of a representation and warranty. I should note the representation and warranty, particularly the no untrue statement representation and warranty, is the same one that Aurora

received from the entities from which it purchased loans, is set forth in Aurora's seller guide, same representation and warranty. Virtually the same and the same material and adverse effect language.

Here is a letter signed by Mr. Trumpp on Lehman Brothers letterhead verifying income through the work number.

Here is one relying on a reverification of the borrower's employment at the time that notice of breach was being provided.

Next is a letter from Mr. Trumpp on Lehman Brothers' letterhead to an obligor, Belvedere, relying on an Accurint search to establish the borrower's residency.

And then another letter from Mr. Trumpp relying on a credit report to establish undisclosed loan debt.

And then a Bureau of Labor statistics. The relevance of this is that this corroborates what our experts are saying that these types of evidence were used and are used in the industry or commonly and widely used in the industry. And these are the sorts of common disputes that are -- general disputes that are common to groups of loans that we think the Court can resolve.

So we will obviously get into that.

THE COURT: But just go back --

MR. SHUSTER: Yes.

THE COURT: Go back one --

MR. SHUSTER: Of course.

THE COURT: -- slide. So this is an interesting one, right? So the part that you don't highlight, it looks like the person indicated that they were earning 6850 a month or 822 a year as a dental lab technician.

MR. SHUSTER: Right.

THE COURT: And then there's a BLS statistic that shows this virtually meaningless range. Right? So the fact that, as you said, it's not that Lehman is saying -- they're rejecting the authenticity of the evidence. But the mere fact that this was used them, I don't necessarily have to say it's good now, right?

MR. SHUSTER: Clearly not. I mean, ultimately, it's for Your Honor to decide. All we can -- I mean --

THE COURT: All you can say is, like, look, they're now saying this is bad but they used this in the past.

MR. SHUSTER: They used it and our experts are going to say that this evidence is reliable. You know, it's not used in all cases but we do use it in a certain number of cases to establish income. Your range -- that's an unusually wide range for BLS. But BLS provides an income number at different percentiles. I don't -- I think it's 60, 75 and 90. So generally, when we -- when we use it,

we're always using the 90th percentile. So we're assuming that we're at least at that level. Ultimately, of course, it's for the Court to decide. But the fact that we have a blanket outright rejection of this type of evidence which is, we think, a little difficult to square with the fact that when pursuing its own put-back claims, the evidence seemed to be good enough. And --

THE COURT: Okay.

MR. SHUSTER: So the so-called on-hold loans, this is simply a breakdown of how many were on hold and how many were not. And it's not the case that -- well, let me start with the protocol. The protocol describes -- the protocol order describes what a mortgage file shall include. And it says, at a minimum, all the loan documents the RMBS trustees received. There's no suggestion that the trustees failed to comply with that and failed to turn over all of the documents that they received from the various servicers.

The trustees went back and forth and back and forth with the servicers and where they could not obtain documents, the servicers told them there are no more documents. They didn't ignore the trustees. They didn't stonewall them. They simply said we're out of paper. We have nothing left.

The protocol order adds that it may include the documentation identified in Exhibit B to the extent such

documentation is available and applicable". Exhibit B is a -- as the Court well knows, is a more itemized list of documentation. But the protocol does not make it mandatory and set as a precondition that every document set forth on Exhibit B must be available in order for a loan to be subject to review in the loan protocol process. And --

THE COURT: Is there a defined -- is mortgage loan file a defined term in the protocol?

MR. SHUSTER: "Mortgage loan file" is a defined term. It is a defined term. I don't remember what that definition says but it's a defined term. So let me -- I'm going to ask one of my colleagues to --

THE COURT: Okay.

MR. SHUSTER: No. Let me see if I can find it. It should be --

(Pause)

MR. SHUSTER: I'll ask one of my colleagues to do that while I continue.

So the idea that these documents are, you know, absolutely necessary in order for a loan file to be reviewed is just not tenable. I mean, do you have -- in these loan files -- we didn't review a loan file and assert a borrower breach unless there was a loan application on the mortgage and a mortgage note and certain other key documents. If you have a borrower who misstated her or his income or misstated

her or his debt and you have something establishing that, you don't kneed a payment history or a servicer note to establish that there was a breach.

Now -- and the only way that these documents are pertinent is if the Court accepts Lehman's argument -- even arguably pertinent, is if the Court accepts Lehman's argument that the trustees are required to establish what caused a default. But --

THE COURT: Well, I think that Mr. Cosenza would say it differently, that you're saying what caused the default. They're saying the continuing existence of an adverse material effect.

MR. SHUSTER: They can -- well, I don't know if that's how they articulate it. But even if they do, even if they do, if there's an income breach, there's an income breach. That affects the price of the loan. That affects the value of the loan. That doesn't change. It doesn't change whether -- for most of these cases, we don't have a situation where the loan is still current and paid. So the effect that was there that, for example, Judge Castel found was that there was an effect on price, there was an effect on value, and that was a continuing effect to the time of notice.

But these documents, there's nothing in the Court's protocol order that permits Lehman to simply refuse

to review a loan file if it's missing these documents. They may not be there. The servicer didn't have them. If Lehman thought -- you know, Lehman was certainly -- we made our burden to establish that there was a breach and we put it through the loan protocol, they are free to adduce whatever evidence they wish to adduce to rebuke -- to rebut that breach finding. As they say themselves in their own repurchase letters, if you can provide evidence to rebut our findings, please do so. If not, please pay up. But there's nothing in the protocol that says that you could -- that Lehman could give itself a waiver from reviewing a third of the loan files that were put through where the trustees asserted that there were breaches. That's what the servicing notes and the borrower payment histories go to.

The other documents -- now we're talking about the corporate expense reports. Those are expense logs of the servicer and loss certifications where the servicer certifies the amount of loss on a loan. That information is reflected in the remittance reports that are provided to investors in the trusts. Those are what -- and our expert will testify those are what the -- our expert used to calculate purchase price. Those reports go to investors. It is specified in the prospectus supplements for these transactions that remittance reports will be provided to investors. It's called for by the governing documents which

make express that the trustees can rely on remittance reports. But moreover, those reports are sufficient to tell an investor your certificates are wiped out. Your certificates are out of the money. You're holding mezzanine paper that isn't worth a thing. If they're good enough for that purpose, they're good enough for calculating the purchase price on a loan which is all we're talking about. And sure, they may feel -- and the document -- the information that is in the remittance reports comes from the servicer. It comes from the primary servicer. It goes to the master servicer and it goes into the remittance report. Those numbers are built up to, in part, by including corporate expense logs, information from corporate expense logs and loss certifications.

THE COURT: So if I agree with you, right, then I take these 24,000 loans, Lehman says zero. Right? You have a different amount.

MR. SHUSTER: Our amount --

THE COURT: Right?

MR. SHUSTER: Yes.

THE COURT: Yes. You have a --

MR. SHUSTER: Yes. Yes.

THE COURT: You have an amount that ties --

MR. SHUSTER: Decidedly so.

THE COURT: -- to the 24,000 loans.

MR. SHUSTER: Yes.

THE COURT: So then how do I tell what is embedded in that amount on account of what Lehman says is a matured interest --

MR. SHUSTER: Right.

THE COURT: -- right?

MR. SHUSTER: So it's our position -- it's our legal position that we're now claiming the sort of unmatured interest that is foreclosed by 502(c). The purchase price calculation, we say and they say and have said in documents that they filed with the court, is a liquidated damages provision. And in that provision, there is an interest component that is built into it. We're not seeking interest over and above the number that is spit out by the purchase price formula itself. But --

THE COURT: So this is --

MR. SHUSTER: -- if --

THE COURT: -- a liquidated damages amount? It's not an actual damages amount?

MR. SHUSTER: The purchase price calculation is not an actual damages amount. It's a liquidated -- it's a formula for returning -- for returning the loan to the sponsor less whatever has already been received on the loan to the extent that anything has. And --

THE COURT: But I always thought, you know, that

you did liquidated damages when you couldn't calculate actual damages.

MR. SHUSTER: Well, this is -- it's not a calculation of damage. It's a -- it's part of the repurchased protocol. If there's a breach, you take the loan back. This is the formula for how we calculate the purchase price. You don't -- you don't -- there's no causation element in our -- you know, in our review. It's simply a formula for determining what is the number that is applied to that particular loan.

THE COURT: So --

MR. SHUSTER: And --

MR. SHUSTER: -- they have characterized it --

THE COURT: -- in theory then, I could be, if I accept your amount, I won't know whether that -- whether or to what extent that exceeds the actual damages that were suffered by the trustees --

MR. SHUSTER: Well --

THE COURT: -- and the certificate holders?

MR. SHUSTER: -- you will know. You will know. The purchase price formula is fundamentally unpaid principal balance on the loan plus interest plus expenses. So you will know what the actual loss will be because, say, the loan is $400,000, there will be a realized loss on the loan and that's what the purchase price will pick up plus

expenses.

THE COURT: So but -- but let me understand this. And maybe we -- I don't want to get off track. But so if there has been -- there's a breach, something that we can say that's a breach, no argument. But we've got one of these, you know, oh, look, the loan is still performing. Right? You say don't look -- as the wizard of Oz would say, don't look behind the curtain, right? We have a breach. Just look at the breach. So is it possible in that scenario that notwithstanding that interest has continued to be paid and we liquidated pursuant to the formula liquidated here, isn't that going to be a windfall to the certificate holders?

MR. SHUSTER: No, because any interest, like any principal that's already been received, is, by definition, netted out of the calculation. Impossible for that to happen. If that -- that should not happen.

THE COURT: Okay.

MR. SHUSTER: It's not supposed to happen. So no.

But to come back to your --

THE COURT: But will the amount of damages, if you prevail, will that exactly equal to the amount of actual damages suffered by the certificate holders?

MR. SHUSTER: Yes. The actual loss suffered by the certificate holders, yes. It will. Absolutely.

THE COURT: Okay. Why don't --

MR. SHUSTER: That's what -- it will be the realized loss on the loan plus the additional items. But that's what it will be. It will not include any recovered principal, any recovered interest. Absolutely not.

And there's -- so -- but just coming back on this question. Your Honor asked if you disagree with us, is the interest number disaggregated. So in the recent report that -- no. I know. It's Professor Snow. I was trying to remember if it was Professor, Dr. or Mr. -- provided he does disaggregate the interest. So if the Court disagrees with our position, Your Honor will know --

THE COURT: Okay.

MR. SHUSTER: -- how to pull that number out.

So that's our view on the on-hold loans. And then we establish those breaches with the same evidence and we offer that evidence and the same summaries as we do all the other loans. The way we approach those loans, there's no difference except that we assert there's also no defense on those loans. None has been offered.

So coming to materiality. And we have spent a good deal of time discussing materiality so I will -- the material --

THE COURT: Materiality. You mean --

MR. SHUSTER: -- and adverse effect --

THE COURT: --adverse material effect.

MR. SHUSTER: -- standard, yes.

THE COURT: Uh-huh.

MR. SHUSTER: Starts with the language that's in the agreement. And it refers to breaches that materially and adversely affects the value of the related mortgage loan. It doesn't say causes losses on the loan or causes the loss -- the loan to default.

That language has, of course, been interpreted by several courts including Judge Castel who specifically says it means that the breach would have altered the price or increased the risk on the loan and that the trusts need not show that the breach caused a loss or that if there was a loss, it was caused by the breach.

And then Judge Rakoff makes clear that whatever caused the loans to default, if they defaulted, is irrelevant. The issue is that the plaintiff faced a greater risk than was warranted on the loans.

The trustees' experts will testify that the trustees meet their material and adverse effect burden. They have all set forth their opinions in their expert reports.

Mr. Aronoff, I respectfully submit, has more experience in the mortgage industry than anyone by far, than anyone the Court will hear from and certainly more broad-

based experience. He originated loans, underwrote loans, securitized loans, purchased and sold loans. He's done it all in the industry and his experience is broader and deeper than that of anyone else and certainly, with all due respect, Mr. Grice, the plan administrator's principal mortgage industry expert.

Mr. O'Driscoll has extensive and deep experience in the securitization of mortgage loans, mortgage loans securitizations. And he, too, will offer, and has offered, his opinion on the material and adverse effects of the types of breaches that the trustees put forward. And so did Mr. Morrow, who, as I mentioned, has 40 years experience in the origination and underwriting of mortgage loans.

So I referred earlier -- or borrowed earlier from Judge Castel's lexicon. He referred to the sheer size of the disparity and income bespeaks of an intentional misrepresentation. And just to remind the Court, we're looking at misstatements of income and non-disclosures of debt that are of a substantial magnitude. The significance of Judge Castel's referring to intentional misrepresentations, as he says -- His Honor says that if there was an intentional breach, it's almost inherently has a material and adverse effect and a continuing and adverse effect.

THE COURT: Can you put back one slide --

MR. SHUSTER: Of course.

THE COURT: -- please to 91? So these are breaches, right?

MR. SHUSTER: Yes.

THE COURT: Do you know -- what's the then diagram -- what's the overlap between income overstatements and undisclosed debt?

MR. SHUSTER: So --

THE COURT: I don't mean to put you on the spot.

MR. SHUSTER: No, no, no, no. There should --

THE COURT: But these are not -- they're not 28,000 loans here and a different 20,000 loans there. There's some overlap.

MR. SHUSTER: So there is overlap as it's reflected on this chart. And actually, had I noticed that, I might have changed that. But generally, we have -- the way we've organized these is we have 33,000 income breaches. And then there are 17,000 debt breaches that are not overlapping with the income breaches.

So in one of the earlier charts, that's how we set it forth --

THE COURT: Okay.

MR. SHUSTER: -- so the Court can see it that way.

THE COURT: All right. So I don't look at this --

MR. SHUSTER: But here, there are --

THE COURT: I don't add 28 to 20 and get 48,000 loans based on this chart?

MR. SHUSTER: I think this adds up roughly to the same number of roughly 50,000 income and debt breaches. But these charts, there will -- there is some degree of overlap between these charts.

THE COURT: Right. But 50,000 breaches versus 50,000 loans. That's what I'm --

MR. SHUSTER: I'm sorry. This should -- this is -- these are loans.

THE COURT: These are loans.

MR. SHUSTER: These are loans. So we have -- if we go back to the earlier chart that shows the breakdown of income debt, the borrower breaches -- right. So this is non-overlapping as --

THE COURT: Non -- okay.

MR. SHUSTER: -- as to loans.

THE COURT: Thank you.

MR. SHUSTER: Right. Okay.

So coming back to where we are, these are Judge Castel's statements concerning materially and ongoing harm and the harm -- the material and adverse effect that certificates experienced at the time of discovery from the established breaches of income and occupancy.

Now I referred earlier to Lehman's own statements

on this point. And the purpose of this is not to establish a gotcha because, as the Court said a few moments ago, ultimately Your Honor has to decide what Your Honor feels is, you know, reliable evidence and the correct standard. But what I'm suggesting -- what we're suggesting is that Lehman got the standard right here. And that the standard is pretty much four square with what the trustees are saying and what Judge Castel said. In fact, it's more liberal.

And this is not loan specific and context specific. These are broad general statements about the material and adverse effect of an income misrepresentation. The loan can't be sold at full value to another purchaser or a securitization. A substantial discount will be applied. The borrower usually will not be able to pay. The same broad statement is made by Lehman concerning a misrepresentation of mortgage debt.

So it's virtually identical language. And this was -- these statements were submitted by I'll say knowledgeable counsel including counsel sitting to my right. So they know what they're talking about.

And then we have the same sworn -- another sworn declaration concerning occupancy. That's on slide 95. And here, it says that "if a borrower misrepresents his intent to occupy, it has a material and adverse effect for the same reason an occupancy misrepresentation is inherently

material".

So before we get here, just stay at the roadmap. There we go.

So Lehman makes various attacks on the trustees' process some of which I've already responded to. But one of which is that there were errors, that the trustees committed errors. And I will say that in any large loan review, there will be errors. We will show that Lehman made errors. Mr. Grice who criticizes us for making errors made errors. In the MARM case, Judge Castel observes that Ira Holt made errors. That doesn't mean he threw out all of the results of Mr. Holt's review. In the Flagstar case, Judge Rakoff noted that Ms. Walzak made some errors. That's the way it goes.

Moreover, in proposing the protocol to the Court, Lehman actually anticipated errors. It submitted, for example, a declaration from Mr. Pino, the head of Recovco, and he said, "For document defect claims, such as loan file documents, such as a HUD-1 settlement statement, are allegedly missing or appraisal is allegedly missing, it is my view based on my prior experience" -- and he describes his experience not so much in this document but elsewhere. He says he's done five loan reviews well in excess of a billion dollars and so forth. Recovco's certainly a shop with a lot of experience -- "that the plan administrator

will be able to locate many of the documents asserted in missing".

So, you know, he is saying that based on his experience with large scale loan reviews, there are going to be some mistakes. Mistakes cannot impugn the entirety of the trustees' process. And moreover, most of the mistakes that Lehman and its experts refer to and its witnesses refer to are on the missing document side of the ledger not -- not -- on the borrower breaches side of the ledger. There, there were very few assertions that the trustees incorrectly identified evidence or said that a piece of evidence said something that it didn't say. Exceedingly rare that assertions of errors are made with respect to breaches predicated on borrower misstatements or omissions.

THE COURT: But here, you're telling me that your error rate is really low. Really low. Boy, are you guys good. Right?

MR. SHUSTER: Certainly --

THE COURT: So much so --

MR. SHUSTER: -- on the borrower side.

THE COURT: Right. So much so that the amount that you're seeking is markedly out of line with comparable settlements across prior RMBS cases.

MR. SHUSTER: I'm actually -- I'm --

THE COURT: You're getting there?

MR. SHUSTER: No.

THE COURT: No?

MR. SHUSTER: But I'm glad you asked actually. And it's one of my notes that I wanted to make sure to cover.

THE COURT: Right. So, I mean, there's that -- I won't call it a fact. There's that observation --

MR. SHUSTER: Yes.

THE COURT: -- by the plan administrator.

MR. SHUSTER: Yes.

THE COURT: And then there's the additional observation of comparing these amounts sought now to the amount at which the six trusts were liquidated which Mr. Cosenza --

MR. SHUSTER: Yes. And I -

THE COURT: -- went through line by line and --

MR. SHUSTER: Right.

THE COURT: -- asked me to conclude that, if anything, the plan administrator was being generous. So if you could just --

MR. SHUSTER: Yes.

THE COURT: -- save a few minutes to address those --

MR. SHUSTER: Well, why don't -- if I may --

THE COURT: Sure.

MR. SHUSTER: So first, on the settlements, I'll say three things. One, those are global settlements. This is a settlement but it's not a settlement. As I've said before, this is -- we have agreed on a proceeding to arrive at the actual value of the claims. We didn't agree to discount the claims. We didn't' agree to put a haircut on the claims. That's why I'm perfectly happy with the plan administrator's statement that we're here to determine what actually would have happened with these claims.

THE COURT: Right. And the trustees left a whole lot of money on the table --

MR. SHUSTER: No.

THE COURT: -- in these other cases.

MR. SHUSTER: In those other -- well, there are two things at least about those other cases. One, there were no loan reviews. None.

THE COURT: I stand by statement.

MR. SHUSTER: Well, that -- well, but, you know, there was --

THE COURT: You can't -- I mean, you can't add the -- much as you remind me from time to time about how onerous the protocol was notwithstanding the fact that you today told me you would delighted to participate in the protocol. So a little bit of a change of a characterization than what was said before --

MR. SHUSTER: I'm happy with the evidence we obtained.

THE COURT: -- before you arrived. Okay? You can't take the cost of going through the protocol and add it to the prior recovery rate and still you don't at all bridge -- you know, don't do a lot to bridge the gap between those levels and the other levels. You know, I could make all kinds of observations, valid or not, about the different recovery levels. And here's -- you know, countrywide is a lot higher than city. Whatever.

But --

MR. SHUSTER: Well, but that's why the trustees here, having been through the protocol and knowing what they know about the loans here, were not prepared to settle at a flat number. They wanted the opportunity to prove the actual value of the claims. So there is a difference. But it is significant that in those other global settlements there had been no loan reviews. So that was a decision -- that was made by both sides that they were going to resolve those sets of claims without that.

There were also statute of limitations issues there as Lehman's expert, Professor Fischel, acknowledges that are not present here. And actions haven't been filed. So those cases are at an entirely different stage. Now maybe the parties could have agreed and certificate holders

were free to weigh in, but that's where those ended up. But those are material distinctions. And I will say that Professor Fischel, I'm sure, will have his ups -- our ups and downs with him when he's on the stand. And he's certainly, you know, a very capable and eminent expert witness. But he, in his report, said that in comparing those settlements to this estimation hearing, care must be exercised 'cause this isn't a settlement. It's a hearing to estimate the claims. And there are other differences between those settlements and this one.

THE COURT: Yes.

MR. SHUSTER: The Court will see that.

THE COURT: Okay.

MR. SHUSTER: And then as far as the settled trusts go, the process in those instances is where a trust typically gets below a 10 percent level in terms of what remains in the securitization, the master servicer has the compulsory right to close out the trust and purchase the loans and purchase all the other property in the trust. The trustee doesn't agree with that. They don't negotiate the price. The master servicer is the contractual right to get an appraiser to arrive at a value and the trustee can object to the selection of the appraiser but not to the appraisal. And what the appraiser did in those instances is precisely, he looked at the settlement agreement here. He looked at

the number that Lehman recommended here. And he extrapolated from that to a purchase price for the claims. We don't agree with that appraisal. We don't agree with the number here. But it's far from a concession by the trustees that the claims actually have that value. And it is not -- it's not the sort of arm's length transaction that it was suggested to be. And that's exactly what the appraiser did. I forget his name but that's what he did.

THE COURT: Okay. I'm going to impose on you to try to finish up by 4:30. Can you do that?

MR. SHUSTER: Yes, I can.

THE COURT: Okay.

MR. SHUSTER: I'm going to skip how errors are unavoidable in loan reviews 'cause I've made these points.

The withdrawn loans. I've made the point that the withdrawn loans are overwhelmingly in the missing documents and defective documents in compliance areas. We know that because that's set forth in Mr. Grice's own report in Exhibit 3, if we could just quickly go to that page. But we would respectfully maintain again that there's a clear process distinction between missing documents and a defective document -- the claims that are predicated on missing and defective documents, that is to say, material missing from the loan file and breaches that are proven by affirmative evidence that is either in the loan file or

third party evidence. Very few borrower breaches were withdrawn as this chart shows. And these are points I've already made that the withdrawn loans do not affect the overall presentation. And had we gone through the protocol process, loans and, frankly, groups of loans should have dropped off if the parties joined issue enough. That was the purpose of the protocol was, among other things, to get to a whittling down of the claims.

So Lehman has a high rejection rate. We don't have documents from Lehman's files the way we normally would in a litigation. We have a handful of documents that were made public by the examiner who reviewed files from Lehman and Aurora just for a very narrow period of time, just a little snapshot, for purposes of addressing certain matters. But those documents reveal certain things that suggest, at least, that a two percent breach rate is simply not credible given what Lehman said about its own securitizations.

So, for example, this is a document from Lehman's files. An internal review where it says "Special Investigations" -- that was a unit within Lehman -- "completed the review of 240 LXS loans." They reviewed these loans. In fact, in reviewing loans, they used the statistical sample. They used statistical sampling methodologies which we will see when we go through these documents.

And LXS loans, many of the securitizations here are LXS designated securitizations. And many of the other securitizations come off the same securitization shelf as the LXS securitizations. And their review found that 50 percent of the loans contained material misrepresentations.

It's suggestive. I'm not suggesting it's probative of a breach rate.

Here's an e-mail, an internal Lehman e-mail from January of 2007 which refers to the fact that "In the last four months, Aurora has originated the riskiest loans ever. The industry meanwhile has pulled back. During the time, I can see performance for Aurora-originated loans to become even worse. In looking at the trends on originations and linking them to pay them, the picture is ugly."

Another e-mail -- and I am mindful of the time, so forgive me if I'm rushing through -- from Mr. McKinney to himself which he then forwarded to others. He says "our aggregate LXS performance has worsened versus largest competitor on '06 production" -- mortgage maker is what was one of Lehman's mortgage products. "Worsened versus the largest competitor on '06 production." The largest competitor is Countrywide as designated in the subject line. "That is, we are creating worse performance than sub-prime while the rating agencies assume our performance should be substantially better."

So in the hierarchy of loan products, most of the loans here are Alt-A loans. They're supposed to be of a higher quality than sub-prime loans. And here, the Lehman officer is suggesting that, in fact, the ones they're originating are of a lower quality.

THE COURT: What percent of the loans that we're looking at are Aurora originations? Do you know off the top of your head?

MR. SHUSTER: Over 50 percent.

THE COURT: Fifty percent.

MR. SHUSTER: Over 50 percent.

THE COURT: Over 50 percent.

MR. SHUSTER: I think it's 50,000 of the remaining 72,000 loans are Aurora-originated loans. No?

Huh?

Less than that. Okay. I'll get that number --

THE COURT: We'll get there.

MR. SHUSTER: -- but it's a high number.

THE COURT: It's a big number.

MR. SHUSTER: Yes.

THE COURT: Okay.

MR. SHUSTER: The purchase price, Your Honor, I think we have gone through perhaps in sufficient detail. For purposes of the opening, we're going to have witnesses address that. We do make the point in here that Lehman's

position on interest is an entirely new position that was developed. On the eve of trial, Dr. Cornell, another very capable witness, testified that he learned about that change in position for the first time the day before his deposition testimony.

So let me see where I am. Okay. I'm done pretty much. We say that the claims should be -- are worth 11.4 billion. I have a breakdown there of how you get up to that number, if you accept every last one of the trustees' claims. And I don't feel the need to make a big finish but, you know, this is where we are and this is the way we will present our case to the Court.

THE COURT: Okay.

MR. SHUSTER: Thank you, Your Honor.

THE COURT: Very clear. Thank you very much.

Okay. So we resume on the 27th after Thanksgiving. Yes? At 10 o'clock in the morning?

MR. COSENZA: Yes.

THE COURT: Okay.

(Pause)

THE COURT: So as we go through this, there will be variations in start times that come up from day to day so that I can accommodate various urgent matters that have a way of arising. I'll do my best to keep those to a minimum.

Today, for example, I have a full calendar

tomorrow. So I have to ask you to totally clean up. Most nights you won't have to do that. I'll just kind of ask you to tidy up as opposed to fully clean up. I'm going to try to make this as easy for you as possible.

So thank you very much. That was very interesting and detailed and wonderful. And have a happy Thanksgiving to those of you who may not come back next week.

(A chorus of thank you)

THE COURT: Thank you.

(Whereupon, these proceedings were concluded at 4:26 p.m.)

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I N D E X

C E R T I F I C A T I O N

We, Dawn South, Sheila Orms, and Lisa Beck certify that the foregoing transcript is a true and accurate record of the proceedings.

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